

1 UNITED STATES DISTRICT COURT
2 DISTRICT OF NEW JERSEY

3
4 MARY ANN SIVOLELLA, et al,
5 PLAINTIFFS

6 Vs. CIVIL NO.
7 11-4194 (PGS)

8 AXA EQUITABLE LIFE INS. CO.,
9 et al,
10 DEFENDANTS

11 GLENN D. SANFORD, et al,
12 PLAINTIFFS

13 Vs. CIVIL NO.
14 13-312 (PGS)

15 AXA EQUITABLE FUNDS
16 MANAGEMENT GROUP,
17 DEFENDANT

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FEBRUARY 23, 2016
CLARKSON S. FISHER COURTHOUSE
402 EAST STATE STREET
TRENTON, NEW JERSEY 08608

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2 A P P E A R A N C E S:

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SZAFERMAN, LAKIND, BLUMSTEIN & BLADER, PC

5

BY: ARNOLD C. LAKIND, ESQUIRE

DANIEL S. SWEETSER, ESQUIRE

ROBERT L. LAKIND, ESQUIRE

ROBERT G. STEVENS, JR., ESQUIRE

6

MARK A. FISHER, ESQUIRE

CHRISTOPHER S. KWELTY, ESQUIRE

7

CHRISTOPHER S. MYLES, ESQUIRE

FOR THE PLAINTIFFS

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9

BLANK ROME, LLP

10

BY: JONATHAN M. KORN, ESQUIRE

FOR THE DEFENDANTS

11

12

MILBANK, TWEED, HADLEY & McCLOY, LLP

13

BY: SEAN M. MURPHY, ESQUIRE

ROBERT C. HORA, ESQUIRE

14

JAMES N. BENEDICT, ESQUIRE

NIKKI NIELSON, ESQUIRE

15

ANDREA HOOD, ESQUIRE

FOR THE DEFENDANTS

16

17

ALSO PRESENT: PATRICIA LOUIE, ESQUIRE

MANAGING DIRECTOR & ASSOCIATE GENERAL COUNSEL

18

AXA EQUITABLE LIFE INSURANCE CO.

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1 I N D E X

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1 THE COURT: Good morning. Please be seated.

2 Any applications?

3 MR. MURPHY: None from defendants, your Honor.

4 THE COURT: Ready to begin?

00:00 5 MR. HORA: Your Honor, Robert Hora for defendants.

6 Defendants called call expert witness, William Holder.

7 THE COURT: All right. Mr. Holder.

8 (WILLIAM W. HOLDER, sworn)

9 THE DEPUTY CLERK: State your name for the record.

00:00 10 THE WITNESS: William Wallace Holder.

11 THE COURT: Once you're seated, sir, could you just
12 spell your last name for us?

13 THE WITNESS: Certainly, it is H-o-l-d-e-r.

14 (DIRECT EXAMINATION OF WILLIAM HOLDER BY MR. HORA:)

00:01 15 Q. Mr. Holder, what is your current occupation?

16 A. I serve as Dean of the Leventhal School of Accounting at
17 the University of Southern California, and also teach and
18 serve as professor there.

19 Q. Could you please describe for us your educational

00:01 20 background beginning with college?

21 A. Certainly. I received a Bachelor of Science in business
22 administration degree with a major in accounting, from
23 Oklahoma State University; I then attended the University of
24 Oklahoma where I received a Master of accountancy degree and a
00:01 25 Doctorate in business administration with a dissertation field

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1 also in accounting.

2 Q. Can you just put some dates on that? When did you get
3 your Bachelor's and when did you get the other degrees?

4 A. Certainly. I received my Bachelor's degree in 1969, my
5 Master's in 1972, and the Doctorate in 1974.

6 Q. Could you please describe your academic employment
7 history since graduating with your Doctorate in 1974?

8 A. Certainly. I first joined the faculty at Texas Tech
9 University, I served there for five years, I began as an
10 assistant professor during that period of time, I was promoted
11 to associate professor and granted tenure; during that period
12 of time I also served as a visiting professor at the
13 University of Tennessee.

14 In 1979 I joined the faculty at the University of
15 Southern California as an untenured associate, and since then
16 I've been granted tenure, promoted to professor or full
17 professor, and then I held I think it's three endowed chairs
18 or professorships.

19 Q. So, roughly how long have you been tenured at the USC?

20 A. Well, it would have been since the early to mid '80s, I
21 don't remember the exact date of that grant.

22 Q. And all of those positions that you've been talking
23 about, they've been in the field of accounting?

24 A. They have, yes, sir.

25 Q. Broadly speaking, what have you done as an academic in

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1 the field of accounting?

2 A. Well, the things one would normally expect I think, I've
3 certainly taught financial accounting, managerial accounting,
4 cost accounting, I've taught auditing; over the years, I have
5 conducted research, published the results thereof, I have --
6 and that's generally been in the fields of managerial cost
7 accounting, financial accounting and reporting.

8 I have rendered service both to the university, but
9 also to the profession, serving on policy groups, standards --
10 accounting standards setting bodies over the years; and then
11 in addition to that I've done a good bit of consulting over
12 the duration of my career.

13 Q. You just mentioned financial accounting, what is
14 financial accounting?

15 A. Financial accounting is a functional area of accounting
16 that is designed primarily I think to provide decision useful
17 information to individuals outside a reporting entity, a
18 business enterprise. Those individuals typically lack the
19 authority and the proximity to specify the type of information
20 that they would like to have on which to base their decisions,
21 primarily investment and credit decisions.

22 The financial accounting information is also commonly
23 used internally within organizations, business enterprises,
24 but it's designed primarily for those that are outside the
25 organization.

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1 Q. Could you describe broadly for us what you've done in the
2 area of financial accounting?

3 A. Sure. I have taught in that area, I've written in that
4 area, I've conducted research in that area and published;
5 again, I mentioned the standards setting activities, financial
6 accounting generally encompasses a rather large range of
7 professional accounting standards that one must follow for
8 financial information to be presented in conformity with GAAP.
9 And I served on several of those accounting standards setting
10 groups over the years.

11 I've written textbooks or co-authored at least
12 textbooks in financial accounting that was published through
13 five editions used at numerous colleges and universities; I
14 still am involved in publishing a practice manual, which
15 guides audits of financial information presented in conformity
16 with generally accepted accounting principles.

17 Q. And the textbook you just mentioned, what is that?

18 A. Its title is Intermediate Accounting, it deals with -- or
19 dealt -- it deals with a wide range of financial accounting
20 and reporting topics.

21 Q. Are you familiar with something called the SEC and
22 Financial Reporting Institute?

23 A. I am, yes.

24 Q. Could you explain what that is?

25 A. That institute is an organization within the Leventhal

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1 School of Accounting at USC, it does a number of things over
2 the years; it's commissioned research, one of those projects I
3 and a couple colleagues participated in; it also hosts
4 so-called round tables, when there are major issues
5 confronting the profession, we can act as an independent forum
6 for practitioners and business executives to meet and confer
7 with regulators, standard setters, or individuals of that ilk,
8 and it provides a good forum for an interchange of ideas.

9 We also hold an annual conference that attracts 6 or
10 700 pretty much senior executives in business enterprises,
11 partners from public accounting firms; and the presenters at
12 that conference are -- we've been very blessed, they're
13 individuals such as the chairman of the financial accounting
14 standards boards, the chief accountant of the SEC,
15 commissioners of the SEC occasionally as the chair person.

16 Q. And you mentioned a little bit earlier in your testimony
17 that you served on accounting standard setting bodies?

18 A. I did.

19 Q. Could you flesh that out a little bit for us?

20 A. Sure. I served originally as the senior technical editor
21 of an industry accounting and audit guide, dealing with audits
22 of state and local government units; I also then served on a
23 compliance auditing task force that focused on the auditor's
24 responsibility for identifying violations of laws and
25 regulations in the related disclosures in financial statements

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1 for those. I then served on a group called the accounting
2 standards executive committee; that was a group that published
3 a variety of different types of standards. We issued
4 statements of position accounting and audit guides; other
5 documents, practice bulletins and so on, that in part
6 established generally accepted accounting principles.

7 That worked focused on a wide range of entities. We
8 set -- during my time on the committee, we set accounting
9 standards for everything from common interest realty
10 associations to insurance companies, mutual funds and so on,
11 as well as other financial institutions, banks, savings and
12 loans.

13 Q. And when were you on that committee?

14 A. That was from '87 to '90.

15 Q. Have you had any other roles with accounting standards
16 setting bodies?

17 A. I have. I served two five-year terms on the governmental
18 accounting standards board that started in 2000, and ended in
19 2010. That group sets generally accepted accounting
20 principles for the nation's 80,000 or so units of state and
21 local government.

22 Q. Now, you mentioned generally accepted accounting
23 principles a couple of times; what is that or what are they?

24 A. Sure. Generally accepted accounting principles
25 represents a body of knowledge composed I would say primarily

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1 of written accounting standards, with which information
2 contained in financial reports must comply, if those financial
3 -- resulting financial statements are to be presented in
4 conformity with generally accepted accounting principles. The
5 Securities and Exchange, for example, requires SEC registrants
6 generally to prepare their information in conformity with that
7 body of knowledge, in conformity with generally accepted
8 accounting principles.

9 Q. And who forms generally accepted accounting principles?

10 A. Over the years a large number of or relatively large
11 number of organizations have performed that function. The SEC
12 was formed back in the early '30, and one of the first things
13 they did was they had the authority to set accounting
14 standards; they delegated that authority to the private sector
15 and a number of organizations over the years, including AcSEC,
16 has been active in writing those accounting standards.

17 MR. STEVENS: If I just may object; you used a
18 phrase there AcSEC --

19 MR. HORA: I was just going to get to that.

20 BY MR. HORA:

21 Q. You used an acronym and I'd like you to explain that.

22 A. I did and I apologize. The Accounting Standards
23 Executive Committee, which I alluded to earlier and on which I
24 had served, was known by that acronym of AcSEC. Sorry.

25 Q. Are you familiar with something called FASB?

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1 A. GASB?

2 Q. FASB, F-A-S-B --

3 A. FASB, yes, absolutely.

4 Q. What's FASB?

00:11 5 A. FASB is the Financial Accounting Standards Board, it is
6 currently the most authoritative standards setter establishing
7 GAAP for business enterprises, and not-for-profit
8 organizations. Such as USC, for example.

9 Q. Have you had any role with FASB?

00:11 10 A. I have, yes. The FASB and the GASB are frequently
11 characterized as sister boards, so during my 10 years were
12 housed in the same building and shared the same facilities.
13 So, during the 10 years I was on GASB many of our projects
14 would have some relationship to -- some interrelationship with
00:11 15 those being pursued by the FASB. So we would discuss those
16 projects among board members of both FASB and GASB or staffs
17 would interact and so on. We both had accounting for
18 derivatives projects going at the same time, so there was a
19 good bit of discussion about those that took place. In
00:12 20 addition to that I was commissioned to do research at an
21 earlier point by the FASB that were designed to help their
22 standards setting efforts.

23 Q. Now, earlier in your testimony you mentioned something
24 called managerial accounting; do you recall that?

00:12 25 A. I do.

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1 Q. What is managerial accounting?

2 A. Managerial accounting is a functional area of accounting
3 that is designed to provide decision useful information to
4 those that manage business enterprises. And there are a
5 number of facets of managerial accounting, cost accounting
6 being one of those; cost accounting also related to financial
7 accounting very closely. But managerial accounting is
8 designed to provide information of use to those that are
9 charged with the responsibility of managing the business.

10 Q. Broadly speaking, could you describe your experience in
11 the area of managerial accounting?

12 A. Sure. Well, again, I've taught in that area, I've taught
13 a number of managerial and cost accounting courses over the
14 years; I also have written in that area, performed research
15 and published information about managerial accounting,
16 contributed to a handbook on cost accounting; I also have
17 consulted on cost accounting issues and learned from those
18 endeavors as well.

19 Q. How if at all does managerial accounting differ from
20 financial accounting, which is what we were talking about a
21 little bit earlier?

22 A. Well, there's a considerable overlap. I think it's a
23 fair to say while financial accounting is required to be
24 guided by professional accounting standards established
25 establishing generally accepted accounting principles, under

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1 managerial accounting you do have more flexibility, you can
2 ask for alternative presentations. I think the managerial
3 accounting body of knowledge recognizes that the decisions
4 that individuals make that manage business enterprises vary,
5 from very strategic long-range focus, to incremental
6 decisions, should we accept this order that's coming in or
7 should we reject it. So there are great many types of
8 decisions that managerial accounting addresses, that really
9 aren't the subject of financial accounting.

10 Q. And you've talked a little bit in your testimony so far
11 about cost accounting, and I'd like to step back a little bit
12 and define that. What is cost accounting?

13 A. Cost accounting generally is the process of associating
14 economic endeavor, that is, the costs that incurred in
15 fulfilling some function, some activity, some good or some
16 service. So cost accounting is the association of economic
17 endeavor with some productive function, some
18 revenue-generating activity, some good, some service.

19 Q. And broadly speaking, could you explain for us what
20 you've done in the area of cost accounting?

21 A. Again, I've taught in that area, college courses devoted
22 to cost accounting, and college courses and university courses
23 that deal in part with cost accounting, concepts and
24 practices; I've also performed research and published in that
25 area; and also consulted over the years in -- on issues of

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1 cost accounting.

2 Q. And generally, without revealing any confidential
3 information, could you describe for us your consulting work
4 with respect to cost accounting?

10:15 5 A. Sure. The earliest involvement involved a hospital. The
6 Medicare formula had just been -- the Medicare program had
7 just been put in place recently, and the whole process of
8 reporting the Medicare and receiving reimbursement for
9 providing services under that program, was cost based; that
10:16 10 is, the cost of providing services to Medicare patients needed
11 to be measured, and that would in large measure determine the
12 amount of reimbursement that a hospital would receive.

13 And so you had a large number of revenue producing
14 departments within the hospital, various varying levels of
10:16 15 Medicare penetration as we would call it, that is, the
16 percentage of patients served that were Medicare eligible; for
17 example, nursing service, which is essentially the room and
18 board, would generally have a higher percentage of Medicare
19 patients, than say something like OB-GYN, older people don't
10:16 20 have babies too much.

21 So the cost -- finding the cost determination for that
22 we would try to allocate the cost of various support
23 departments, like housekeeping and purchasing and human
24 resources and medical records, to those revenue producing
10:17 25 areas for purposes of determining the appropriate

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1 reimbursement for Medicare.

2 Since that time I have worked with other hospitals
3 trying to assist them in developing systems that will allow
4 them to evaluate cost relationships with productive functions
5 they were considering. I've also been involved in terms of
6 cost accounting in the standards setting activities I alluded
7 to. A good deal of cost accounting is found in financial
8 accounting reporting; for example, we had a project on
9 environment contamination remediation obligations and trying
10 to measure the costs that would be incurred by a government in
11 cleaning up a polluted harbor or some other property that the
12 government owned that required remediation, and, of course,
13 you know, there are great many cost allocation problems that
14 are associated with -- with those processes.

15 I've consulted on other issues that involved cost
16 accounting, the costs, for example, of acquiring a building,
17 if you're building it yourself will require -- to construct a
18 building may require cost allocations, frequently does.

19 Q. Have you done any cost accounting work with respect to
20 mutual funds?

21 A. I don't recall doing so, other than in this case in
22 looking at it.

23 Q. How if at all are cost accounting principles and concepts
24 applicable to different industries?

25 A. Well, I think the same general concepts apply almost

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1 regardless of the industry. Again, the goal of cost
2 accounting is to associate the amount of economic endeavor,
3 that is, the costs that were incurred with some financial
4 that's being performed by the organization, and that
5 transcends industries generally.

6 Q. Mr. Holder, have you ever testified before Congress?

7 A. I have, yes.

8 Q. Could you explain when and on what subjects?

9 A. Sure. As I recall that was in May I believe of 2002;

10 Congress at that time was considering legislation that would
11 become known later when passed as the Sarbanes-Oxley Act, they
12 were interested in the nature, extent I guess of alleged
13 fraudulent financial reporting that was occurring in our
14 capital markets. Enron had just failed, Worldcom also had had
15 its problems; the congressional committee before whom I
16 testified was -- they thought well informed about those, so
17 they asked me to look at five other instances that had been
18 reported in the press involving allegations of fraudulent
19 financial reporting and to try to provide insights to them on
20 the causes and perhaps the cures, things that could be done
21 that would mitigate or extinguish instances of fraudulent
22 financial reporting.

23 Q. Have you heard of something called the National
24 Commission on Fraudulent Financial Reporting?

25 A. I have.

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1 Q. What is that?

2 A. That was a commission formed back in the '80s for similar
3 reasons. I think that was probably a response to the -- what
4 became known as the savings and loan crisis, the failure of a
5 great many savings and loans, and financial accounting and
6 reportings role in either not predicting that or not conveying
7 the troubles of a given institution on a timely basis.

8 The commission was named after its chairman, James

9 Treadway was an SEC commissioner, and he chaired that

10 commission, so it became known as the Treadway Commission.

11 But they commissioned themselves a number of research

12 projects, one of which I participated in with two of my

13 colleagues. Our charge was to look at things that the

14 Securities and Exchange Commission could do or do differently

15 that would mitigate or diminish the frequency, severity of

16 instances of fraudulent financial reporting.

17 Q. Thank you. Do you have any professional accreditations?

18 A. Yes, I do.

19 Q. What are they?

20 A. I am a Certified Public Accountant both in California and
21 Oklahoma where I took the examination.

22 Q. And how about a professional affiliations, do you have
23 any of those?

24 A. I do, I am a member of the American Institute of

25 Certified Public Accountants; I'm a member of the California

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1 Society of Certified Public Accountants; I am a member of the
2 American Accounting Association; and then in each of those
3 organizations I've held various offices and served on
4 committees, chaired some of them.

10:22 5 Q. Have you received any awards during your career?

6 A. I have, yes.

7 Q. Generally speaking, what have you received?

8 A. Well, there have been a number of teaching awards and
9 because students propel those that they tend to mean a great

10:22 10 deal to the recipient, they certainly do to me. I've also
11 received awards from professional societies; I've received
12 awards from the two schools from which I graduated, Oklahoma
13 State, the university of Oklahoma; I received the Gold Medal
14 for distinguished service from the American Institute of CPAs;
10:22 15 I also was named for a couple years as one of the hundred most
16 -- I think the phrasing is influential people in accounting.

17 Q. Okay. Mr. Holder, who developed the opinions that you
18 intend to offer today?

19 A. Yes, I did.

10:23 20 Q. You did.

21 A. I did. I'm sorry, I thought --

22 Q. I said who developed. In the process of forming your
23 opinions, did anyone assist you?

24 A. Yes, they did. I was assisted by the professional staff
10:23 25 of Cornerstone Research.

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1 Q. What is Cornerstone Research?

2 A. They are a company that tends to as least focuses, to my
3 knowledge, on economic analysis; they provide litigation
4 support over a wide range of matters and topics and functional
5 areas, including accounting and financial reporting; they've
6 assisted me in numerous engagements I've been involved in, and
7 they did in this one.

8 Q. And why did you obtain assistance from Cornerstone?

9 A. Well, I think there were efficiency concerns at issue. I
10 think they were -- in my experience have been well positioned
11 to provide that kind of assistance. I generally used them as
12 I would use a research assistant on a research project;
13 they're very helpful in organizing information, getting
14 documents, putting them in logical order and so on. But they
15 were -- they were helpful in a variety of ways, in assisting
16 me in developing my opinions.

17 Q. Thank you.

18 MR. HORA: Your Honor, at this time I ask the Court
19 to qualify Mr. Holder as an expert in financial accounting,
20 managerial accounting, and cost accounting, and submit that
21 he's qualified to testify as an expert in these areas by
22 reason of his experience and training.

23 THE COURT: Mr. Stevens?

24 MR. STEVENS: Good morning, your Honor. The only
25 thing I would note is that we had filed prior to this a motion

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1 in limine to preclude his testimony entirely. It's my
2 understanding based on discussions I heard yesterday that the
3 trial schedule and everybody agrees we'll be finished Thursday
4 and that's sufficient time for defendant to put in all its
00:24 5 witnesses; because of that we're going to reserve on that
6 motion, not entertain it at this point and wait for
7 cross-examination to raise the issues that we had identified
8 in that specific motion, your Honor.

9 THE COURT: All right. Do you have any objections
00:25 10 to that?

11 MR. HORA: No objection to that.

12 THE COURT: All right. I guess I'm tentatively
13 finding that Mr. Holder is an expert in financial, managerial
14 and cost accounting.

00:25 15 MR. HORA: Thank you.

16 BY MR. HORA:

17 Q. Mr. Holder, as part of your work in this matter, have you
18 reviewed the process by which FMG reports its profitability to
19 the EQAT, E-Q-A-T, Board of Trustees?

00:25 20 A. Yes, I have.

21 Q. And based on your understanding how does FMG classify
22 sub-advisory and sub-administrative fees in these reports?

23 A. In the reports I've seen they classify those costs as
24 expenses, rather than as a direct reduction of revenues.

00:25 25 Q. Okay. And my next question I'm just going to ask for a

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1 yes or no because I want to lay some foundation later for what
2 your opinion is, but did you reach any opinions about FMG's
3 classification of sub-advisory and sub-administrative fees in
4 those profitability reports?

00:26 5 A. Yes.

6 Q. And could you let us know what you did to prepare
7 yourself in forming your opinion?

8 A. As they relate to this profitability issue, I read a
9 great number of documents; I looked at the arrangements, the
00:26 10 agreement between the Trust and FMG; I looked at the
11 agreements between -- some of the agreements at least between
12 FMG and the sub-advisors and sub-administrators; I had
13 interviews and discussions with Mr. Joenk, Ms. Louie; I read a
14 number of our documents, deposition testimony, trial
00:26 15 testimony; I also conducted analysis of the professional
16 literature of the accounting profession and considered it as I
17 went through my analysis. Those things come to mind.

18 Q. And could you please summarize for the Court your opinion
19 with respect to FMG's classification of sub-advisory and
00:27 20 sub-administrative fees in its profitability reports to the
21 EQAT Board?

22 A. I think the classification as expenses as I've indicated
23 was perfectly appropriate.

24 Q. Now, you mentioned -- one thing you mentioned you looked
00:27 25 at was accounting standards, and I'd like to go through some

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1 of the professional standards that I understand are related to
2 your opinion.

3 MR. HORA: Could we hand the witness DX-1510?

4 Q. Do you recognize this document?

5 A. I do.

6 Q. What is it?

7 A. This is the text of an Emerging Issues Task Force
8 consensus abstract, that's what EITF at the top left stands
9 for, and it was issued in 1999. It was the 19th abstract they
10 issued that year, so it's characterized this EITF 99-19.

11 Q. And this is a document that Mr. Barrett cited in his
12 report; correct?

13 A. I recall that being the case, yes.

14 Q. What is the Emerging Issues Task Force?

15 A. That is a group of practitioners, business executives, as
16 well as those in public accounting practice, established by
17 the FASB to deal with problems that were -- or challenges that
18 were arising in practice, there may be new transactions, there
19 may be into business structures; when those arise the EITF is
20 to provide immediate guidance if you will to the practicing
21 community, to the accounting profession.

22 The FASB in establishing its standards, goes through a
23 rather lengthy due process procedure, some of those can take
24 five, seven, eight years. And so the EITF was designed to be
25 -- to provide much more immediate guidance to emerging issues,

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1 trends, things that are taking place in practice that are new.

2 Q. Now, on this document in brackets it says, superseded by

3 FASB codification 9/15/2009; do you see that?

4 A. Yes.

10:29 5 Q. What does that mean?

6 A. Well, as I testified earlier, there have been a very

7 relatively large number of standards setting organizations

8 over the years, and the standards they issued have all

9 different kinds of names; there was no central electronic

10:29 10 repository for all of those standards, it was difficult to

11 search, using keywords and so on, there wasn't a single

12 electronic database for all of the accounting standards.

13 So the FASB recognized that it would be highly

14 desirable to create such a database. They set about doing so,

10:30 15 and in 2009 they codified all the existing authoritative

16 standards into that single accounting standards codification.

17 And so they took a great many, including EITF 99-19, a great

18 many existing standards and just arranged them into a single

19 database that was much easier to search and use and identify

10:30 20 the pertinent literature.

21 Q. And did the substance of EITF 99-19 change when it was --

22 change when it was codified by FASB in 2009?

23 A. It did not.

24 Q. So it's still the same.

10:30 25 A. Pardon me?

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1 Q. It's still the same.

2 A. Yes.

3 Q. All right. And could you let us know what the EITF 99-19
4 addresses?

10:30 5 A. Well, it addresses circumstances in which there may --
6 there may have been deviations in practice or different
7 practices beginning to emerge for the circumstances in which
8 revenue would be reported gross with certain costs reported as
9 expenses, and circumstances in which revenue would be reduced
10:31 10 by those costs and not then reporting those costs as expenses.
11 There were a number of emerging issues here that I think
12 probably captured the task force's attention and caused them
13 to prepare this particular standard.

14 And so it's essentially provided in here are -- first
10:31 15 of all, considerable professional judgment is recognized as
16 necessary; and then secondly, there are a number of indicators
17 that are established that would mitigate toward reporting
18 those costs as expenses versus reporting them as reduction of
19 revenue.

10:31 20 Q. And just to make this a little more tangible, can you
21 give us an example of a situation where this guidance would
22 apply to the issue of reporting revenues gross versus net?

23 A. Sure. There are a couple of that come to mind. In
24 retail, for example, there may be instances in which a
10:32 25 retailer does not actually buy goods that are sold within its

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1 premise, those goods are put on racks by another party, and
2 but yet they're sold through that store. And the retailer
3 never takes possession or owns that inventory, if you will,
4 they don't have the risk of the inventory becoming obsolete,
5 they don't have to pay for the inventory regardless of whether
6 they sell it or not; and then there are other instances in the
7 same store in which they do buy the items that are being held
8 for resale, and they do have those risks of owning the
9 inventory.

10 And so both items go through the cash register when
11 people buy them, but should one of those items be reported as
12 a commission, if you will, for selling someone's else's goods
13 or services, or should they be reported as the total revenue
14 accruing to the -- to the retailer. Amazon.com was one of the
15 organizations I think that probably helped propel this. When
16 you order something from Amazon.com, in some circumstances at
17 least, you may send them \$40, and what they do is arrange for
18 a book to be sent to you and pay the book seller the \$32 for
19 the bookkeeping only the 8. And questions arise as to whether
20 in a circumstance like that where Amazon did not acquire the
21 book and have the risk and rewards of the ownership of the
22 inventory of books, should that be reported as a commission or
23 did they generate \$40 of revenue. And so it's those kinds of
24 questions; how much revenue should be reported here, 8 or 40
25 in that case.

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1 Q. Mr. Holder, I think you pushed the microphone away from
2 yourself a little bit.

3 A. I'm sorry.

4 Q. All right. Could you turn to page 2 of DX-1510,

00:34

5 Defendant's Exhibit 1510. And I want to specifically focus
6 you on the first sentence of paragraph 3. Just let me know
7 when you're there.

8 A. I'm there.

9 Q. All right. Could you read that sentence?

00:34

10 A. Yes. It says: The issue is under what circumstances a
11 company should report revenue based on: (a) the gross amount
12 billed to a customer because it has earned revenue from the
13 sale of goods or services, or (b) the net amount retained,
14 that is the amount billed to the customer less the amount paid
15 to a supplier, because it has earned a commission or fee.

00:34

16 Q. And I'd like to understand how some of the terms in that
17 sentence apply to the case here as you understand it.
18 Focusing again on the first sentence of paragraph 3, what is
19 the company here?

00:35

20 A. The company here would be FMG.

21 Q. And who or what are the customers?

22 A. The customer here would be the Trust, the funds
23 themselves.

00:35

24 Q. And who are the -- who are the suppliers as you
25 understand it here?

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1 A. The supplies here would represent the sub-advisors and
2 sub-administrators.

3 Q. All right, thank you. Let's turn to page 4 of
4 Defendant's Exhibit 1310 -- 1510. And there's a heading there
5 that says Indicators of Gross Revenue Reporting. Do you see
6 that?

7 A. I do, yes.

8 Q. And just briefly -- because I think you kind of went over
9 it already, what's gross revenue reporting?

10 A. Well, where you have this cost from a supplier, and it's
11 not clear in your own mind whether it should be reported as an
12 expense, or whether it should be reported as a direct
13 reduction of revenue, these eight indicators are designed to
14 provide guidance in resolving that question.

15 Q. All right. And have you summarized these eight
16 indicators of gross revenue reporting in a demonstrative?

17 A. I have.

18 MR. HORA: Okay. We hand the witness Defendant's
19 Exhibit 2053.

20 And, your Honor, before I move into that document, I
21 would like to offer in evidence Defendant's Exhibit 1510.

22 THE COURT: Any objections?

23 MR. STEVENS: No objection, your Honor.

24 THE COURT: All right, admitted.

25 (Defendant's Exhibit 1510 was marked into evidence.)

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1 BY MR. HORA:

2 Q. So, Mr. Holder, I take it you have in front of you

3 Defendant's Exhibit 2053?

4 A. I do.

00:37 5 Q. Was this a document that was prepared under your
6 direction?

7 A. It is, yes.

8 Q. What's the purpose of this demonstrative?

9 A. Well, it's designed to summarize the general guidance and
00:37 10 provisions of the EITF we've been discussing, and apply
11 those -- those criteria or actually the indicators to the
12 relevant circumstances in this matter.

13 Q. What information did you use to prepare this document?

14 A. Well, certainly the mitigator -- or indicators that are
00:37 15 contained in the EITF document were used by me; in addition to
16 that, the documents that I've alluded to earlier in large
17 measure are the ones that I used in preparing this exhibit.
18 So, those would be the agreement between the Trust and FMG;
19 the agreements between FMG and some at least of the
00:38 20 sub-advisors and sub-administrators; the interviews and
21 discussions I've had with Mr. Joenk particularly and Ms.
22 Louie; trial testimony that I've read of this matter;
23 depositions, other documents come to mind.

24 Q. Sure. And could you walk us through your analysis with
00:38 25 respect to the eight indicators of gross revenue reporting?

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1 A. Certainly. You can see that there are eight here, you
2 can also see that item 2 and item 7 I did not find applicable,
3 because here in this case we're talking about services rather
4 than tangible inventory items that, you know, where you really
5 wouldn't have that kind of a risk in either 2 or 7. So there
6 were six of these that I found to be of relevance.

7 And the following pages in the exhibit, there's one for
8 each of the six that are relevant. So the first indicator is
9 that the entity in this case, FMG, is the primary obligor.

10 And so if you look at the second page, you can see just a
11 couple of examples that I picked from the information of which
12 I was aware, that support that the entity, FMG here, is the
13 primary obligor to the Trust and the funds. So they -- the
14 question is whether they have accepted the obligation to
15 provide these services, or merely the obligation to arrange
16 for services say to be provided.

17 And so here, some of the language I've chosen to
18 present, the Trust hereby appoints the manager, that's FMG, as
19 the investment manager for each of the portfolios of the
20 Trust; and then FMG accepts such appointment and agrees to
21 render the services and assume the obligations. In the
22 administrative side of it you find similar language; the Trust
23 hereby appoints FMG to provide administrative, accounting and
24 compliance services, and FMG accepts such appointment and
25 agrees to furnish the services.

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1 Speaking as an accountant and trying to interpret this
2 agreement and apply the accounting indicators to it, this
3 suggests to me, and it's consistent with other evidence I
4 recall, the testimony and so on, that indeed FMG was
5 responsible for the provision of the services and not just for
6 arranging someone else to provide them.

7 If you look at two -- or I'm sorry, the third one, the
8 second one is not applicable; it says the entity, FMG in this
9 case, has latitude in establishing price. And so if you look
10 at the third backup, you can see that FMG has negotiated with
11 the Trust in those agreements, and that the Trust will pay the
12 manager, FMG, with respect to each portfolio the compensation
13 that's specified in the agreement. And you see similar
14 language on the administrative side. So, it appears here that
15 FMG was involved in establishing a price rather than say --
16 with the Trust, rather than say the sub-advisors or
17 sub-administrators.

18 If you look at the fourth one, here FMG changes the
19 product or performs part of the service. And so, I'm aware of
20 the information here, and again these are examples that I've
21 chosen to include on this exhibit. But FMG will have overall
22 supervisory responsibility for the general management and
23 investment of each portfolio's assets; full discretion to
24 select new or additional sub-advisors; FMG will -- is to
25 assess each portfolio's investment focus and seek to implement

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1 decisions with respect to the allocation/reallocation of the
2 portfolio's assets among sub-advisors; FMG is to monitor
3 compliance of each sub-advisor with the investment objectives,
4 policies and restrictions; and FMG will also furnish to the
5 Trust office space, personnel, preparation of prospectus and
6 other documents.

7 So -- and you find similar language over on the
8 administrative side. And so I think it's clear here that FMG
9 is involved in the providing of these services and assuring
10 that the services are of the quality that is necessary to
11 appropriately operate the funds.

12 If you look at the fifth one, does the entity, FMG in
13 this case, have discretion in selecting the suppliers. And so
14 if you look at number 5, you can see here that FMG will at its
15 own expense select and contract with one or more sub-advisors.
16 Also, FMG will have full discretion to select new or
17 additional sub-advisors for each portfolio. And you find
18 similar language I think in the administrative side.

19 And so, this suggests that strongly, that FMG does have
20 the ability to pick the sub-advisors, sub-administrators at --
21 at their discretion.

22 In 6, the entity FMG is involved in the determination
23 or product or service specifications. And so if we turn to
24 the sixth item, again, we find language here that FMG has
25 overall supervisory responsibility for general management,

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1 investment of each portfolio's assets; full discretion, again,
2 to select new additional advisors; full discretion to enter
3 into and materially modify existing advisor agreements; full
4 discretion to terminate and replace any advisor and full
00:44 5 investment discretion to make all determinations with respect
6 to the investment of a portfolio's assets not then managed by
7 an advisor.

8 Over on the administrative side it points out the
9 division of FMG's duties and obligations, hereunder between
00:44 10 those to be delegated and those to be performed, shall be in
11 FMG's sole discretion and may be changed from time to time by
12 FMG.

13 Again, the seventh one I didn't find applicable. The
14 eighth one is that the entity FMG has credit risk. That
00:44 15 essentially means if they don't get paid by the Trust, are
16 they still obliged to pay the suppliers, in this case the
17 sub-administrators and sub-advisors.

18 And again, speaking as an accountant interpreting this
19 and trying to apply it from an accounting perspective, you
00:44 20 find that in the agreement the Trust acknowledges and agrees
21 that it is -- it is contemplated that FMG will at its own
22 expense select and contract with one or more investment
23 advisors. And you find similar language in the administrative
24 side; the compensation of the sub-administrator shall be paid
00:45 25 by FMG, and no obligation shall be incurred on behalf of the

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1 Trust in such respect. That suggests to me that FMG does
2 indeed have credit risk here with respect to the two sets of
3 general arrangement.

4 And so, that suggests that the indicators of gross
5 revenue reporting have generally been met here insofar as
6 they're generally applicable, and based on the evidence of
7 which I'm aware.

8 Q. So, Mr. Holder, what's your overall conclusion with
9 respect to how these factors apply to FMG's classification of
10 sub-advisory and sub-administrative fees as expenses?

11 A. Well, I recognize that the information is being reported
12 here to the Board, and that one is not completely bound by
13 generally accepted accounting principles in providing that
14 information. However, I'm also quite aware that when
15 standards setters focus on an issue such as this, they are
16 focusing on the substance of the transaction, the economic
17 realities of the transaction as they perceive it and see it,
18 and that they try very hard to propound accounting standards
19 that will be representationally faithful to what's taking
20 place in the real world; that is, the manner in which these
21 transactions are presented on paper is a faithful
22 representation of what's transpiring in the real world with
23 the rights and risk of the transaction bearing from
24 transaction to transaction.

25 And so, I find this is very supporting of the

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1 reasonableness of presenting these costs, the sub-advisor and
2 sub-administrative costs, as expenses, rather than as
3 reductions in revenue.

4 Q. And by the way, how are sub-advisory and
5 sub-administrative fees reported in FMG's audited financial
6 statements?

7 A. They're reported as expenses there, too.

8 Q. And how if at all did that classification inform your
9 opinion in this matter?

10 A. Well, it certainly supports it. Those financial
11 statements were audited by PricewaterhouseCoopers, the amounts
12 involved I think are material, and so I take comfort from and
13 influence by the accounting treatment that was attributed
14 there, and Pricewaterhouse's unqualified or clean opinion on
15 those -- those financial statements.

16 Q. Now, those financials are an example of financial
17 accounting, not managerial accounting; right?

18 A. That's true, they -- the assertion made is that the
19 figures that are presented in conformity with GAAP.

20 Q. Right. And what's presented to the Board, FMG's
21 profitability calculations, that's an example of managerial
22 accounting; right?

23 A. I think that's a fair statement, yes.

24 Q. Okay. And plaintiffs have asserted in this litigation
25 that the GAAP guidelines that we've been discussing so far,

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1 specifically relate to financial accounting and have nothing
2 to do with how FMG should report revenues and expenses to the
3 EQAT Board. What's your reaction to that?

4 A. Well, I disagree with that.

10:48 5 Q. Why is that?

6 A. Well, I think nothing to do is a rather an extreme
7 statement. I think -- for some of the reasons I already
8 articulated, that when accounting standards setters focus on
9 how a transaction should be reported, that they focus on the
10 substance of the transaction; they try to have replicated on
11 paper the economic realities, the economic substance of what's
12 transpiring in the real world. I do not believe that is
13 dissonant with what the goals would be in reporting to the
14 Board.

10:49 15 So I think one providing information to the Board would
16 certainly consider the application of these standards, the
17 contents of these standards, the philosophies, if you will, of
18 financial accounting and reporting that are embodied in them.
19 Because the goals are rather simple, that is to focus on the
20 substance of what's happening.

10:49 21 Q. And plaintiffs' expert, Mr. Barrett, has testified at
22 this trial that classifying sub-advisory and
23 sub-administrative fees as expenses and reporting
24 profitability to the EQAT Board does not reflect the true
25 economics of the transaction; do you agree with that

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1 statement?

2 A. I do not.

3 Q. Why not?

4 A. Well, because I think probably the best articulation of
5 the substance of the transactions and how they should be

6 accounted for when that substance is identified and subjected
7 to analysis, is probably contained in the EITF pronouncement

8 that we've just been discussing. That I think is important

9 evidence as to what the substance of transactions are, and

10 when you apply those criteria generally to the arrangements

11 here, I think you're inexorably driven to the conclusion that

12 reporting them as expenses is at least perfectly appropriate,

13 if not the preferred or only acceptable way.

14 Q. And as a matter of managerial accounting, do you think

15 it's appropriate for FMG to classify sub-advisory and

16 sub-administrative fees as expenses?

17 A. Yes, I do.

18 Q. All right. Mr. Holder, do you know how the sub-advisory

19 and sub-administrative fees are physically paid?

20 A. I do have that understanding, yes.

21 Q. And what's your understanding?

22 A. My understanding is that the Trust for the funds,

23 disburses cash directly to the sub-advisors and

24 sub-administrators.

25 Q. And do you have an understanding of at whose direction

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1 the Trust does that?

2 A. If I recall correctly, it's at FMG's, yes.

3 Q. Okay. And so instead of having the Trust send the entire

4 management and administrative fees to FMG, FMG directs

00:51 5 payments of the sub-advisors and sub-administrator directly

6 from the Trust account?

7 A. Yes.

8 Q. Okay. Now, does that payment mechanism affect your

9 opinion as to the appropriate classification of sub-advisory

00:51 10 and sub-administrative fees?

11 A. It does not.

12 Q. Why not?

13 A. Well, I think it's ministerial in nature, I think it's

14 clerical in nature, I think frankly it's non-substantive in

00:51 15 nature. There are analogies one can easily develop and

16 articulate that I think parallel this circumstance and

17 illustrate why that's not a particularly important feature of

18 what's transpiring.

19 Q. Could you give us some examples or analogies?

00:52 20 A. Well, I mean if -- to make it a personal example, if

21 you're being paid -- if your compensation your salary is

22 \$200,000 a year, and you authorize your employer to withhold

23 from your salary let's say 10,000 and pay that to a healthcare

24 provider to provide insurance, health insurance for you, that

00:52 25 doesn't lower your compensation to 190,000, you're still

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1 receiving \$200,000 compensation, you're incurring an expense
2 of 10,000; in that case the compensation of 10,000 is paid on
3 your behalf by your employer, but the fact that it's not paid
4 to you and then -- the fact that it's not paid to you and that
5 you pay the insurance company, doesn't have any impact on your
6 gross revenue, your gross revenue is the stated salary amount.

7 Q. Thank you.

8 MR. HORA: Unless your Honor has any questions, I'm
9 going to skip -- shift gears here.

10 THE COURT: No.

11 Q. All right. Let's talk a little bit more about cost
12 allocation which you touched on a little bit earlier.

13 A. Certainly.

14 Q. Mr. Holder, are there any accounting requirements for a
15 cost allocation methodology to be considered a reasonable
16 methodology?

17 A. There are.

18 Q. And could you explain that a little?

19 A. Sure. Essentially there are two broad requirements. One
20 is that the cost allocation methodology adopted be rational,
21 and that is that it makes sense at some level. And while some
22 cost allocation processes are, you know, very obvious, others
23 are much more subjective; but regardless, the cost allocation
24 methodology needs to be rational at some level, that makes
25 sense.

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1 Secondly, the cost allocation methodology must be
2 systematic, and essentially that means it's replicable that
3 other individuals can come out, apply the same cost allocation
4 methodology, and reach similar or identical results.

00:54 5 Q. All right. And is cost allocation a science?

6 A. I believe it to be an art.

7 Q. And why is that? Could you flesh that out for us a
8 little bit?

9 A. Well, yes, because of the inherent subjectivity and
00:54 10 ambiguity that exists in many many situations in which one is
11 trying to attribute economic endeavor or cost to a given
12 activity, I think there are a number of processes, a number of
13 methodologies that would be appropriate to use in essentially
14 identical circumstances. And therefore, the selection of what
00:54 15 one to use becomes a matter of the professional judgment of
16 the information preparer, and consequently, you know, you can
17 have similarly situated professionals applying judgment to the
18 same facts and at least times coming to different conclusions
19 and neither can necessarily be said to be wrong.

00:55 20 Q. Okay. Could you -- would it be possible to give us sort
21 of a real world example that would bring this to life?

22 A. Well, sure. There are a great many, I think that can do
23 that. I mean something as simple as perhaps potentially
24 unremarkable is going to the store and buying a quart of milk;
00:55 25 if you pay a dollar 50 for that quart of milk and you bring it

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1 home in and put it in your refrigerator, and you're going to
2 have on your cereal tomorrow morning, the question might arise
3 what's the cost of that milk. And certainly the cost would
4 include the dollar 50, but it would include many other costs,
5 as least from the perspective of accounting concepts; it would
6 include the cost of traveling to the store, and that would
7 involve if you drove your own car, depreciation on the car,
8 fuel cost, repair cost, you're burning rubber off the tire of
9 the car a little bit; it would require an allocation for the
10 value of your time; the cost of the labor involved in fetching
11 it; when you get home you're storing it for a while, that
12 would involve the cost of utilities; there are also other
13 things in your refrigerator that are been being kept cool, so
14 you would have to allocate that electrical cost to all of
15 those items.

16 And then it gets even more complex. If while at the
17 store you decide well, yes, I need not just milk, but I need
18 razor blades, so you bring two things home; does that cut in
19 half the cost of travel and so on for the milk. I mean the
20 world that we're talking about here in this case, is far more
21 complex than the simple example that I've provided here. But
22 I think one can see that a lot of cost allocations are going
23 to involve subjective determinations.
24 Q. Sure. And what limitations, if any, exist when choosing
25 a cost allocation methodology?

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1 A. I'm sorry; could I --

2 Q. Sure. What limitations, if any, exist when choosing a
3 cost allocation methodology?

4 A. Well, there are a number: The availability of data; the
5 existence of cost drivers, does this cost result from directly
6 the activity that is under analysis; cost benefit limitations
7 certainly apply; the cost of acquiring data may see the
8 benefit from flows from acquiring it, if a less costly method
9 of cost allocation can be adopted, that doesn't result in

10 materially in early -- in materially different allocations
11 from one that costs more, one would -- would select the least
12 costly approach; of course, without doing both you really
13 don't know which is which. But those are -- some of the
14 complex judgments that cause people to pick one cost
15 allocation methodology versus another.

16 Q. And you mentioned cost drivers in your last answer;
17 what's a cost driver?

18 A. A cost driver is a function, an activity that causes a
19 cause to increase, is there a direct cause and effect.

20 Q. Sure. And how if at all does the availability of cost
21 drivers effect the design of an allocation methodology?

22 A. Well, the cost accounting literature I think is fairly
23 clear in providing guidance here. I think there's a
24 preference for cost drivers if they exist, if they're

25 available, to use as a basis for allocating cost. The problem

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1 arises is that in many cases cost drivers simply don't exist,
2 but to the extent they do I think it's preferable that they be
3 used.

00:59

4 Q. And so what do you do if a cost driver doesn't exist or
5 isn't available?

00:59

6 A. Well, you must move to other allocation processes. If
7 the overarching goal is to estimate the cost of providing a
8 function or the cost of providing a good or a service, then
9 all of the costs that are necessarily incurred to provide that
10 good or service need to at least in part be attributed to that
11 good or service. And so less and less direct methods of
12 allocation must be selected. This issue, this challenge is
13 identified in the cost accounting literature and developed at
14 some length.

00:59

15 Q. Okay.

16 A. And the path forward to finding other allocation bases.

17 Q. And we'll look at some in a little bit. Are you familiar
18 with something called time and motion studies?

19 A. I am.

01:00

20 Q. What are they?

21 A. Well, time and motion studies are designed to determine
22 the effort it takes to fulfill a given task --

01:00

23 MR. STEVENS: Your Honor, I just want to object at
24 this point; I believe this is outside the scope of his expert
25 report.

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1 MR. HORA: I certainly don't think so. He's got a
2 huge section in his report about cost allocation methodologies
3 and how they're developed.

4 THE COURT: So this is one element to that?

01:00 5 MR. HORA: Yes.

6 THE COURT: All right. So you may proceed.

7 BY MR. HORA:

8 Q. I think I was asking you what are time and motion
9 studies.

01:00 10 A. Yes, I think I had gotten to the point in my answer that
11 I was going to say they are most useful when the endeavor
12 being evaluated, is of high volume and of repetitive nature.
13 And so you're doing the same thing, one, a worker is doing the
14 same thing over and over and over again; and doing a time and
01:01 15 motion study provides evidence about the time it takes for a
16 particular function to be done. These can become very
17 granular and frequently are.

18 I recall a consulting -- or an engagement in which I
19 was involved, involving a manufacturer of children's clothing,
01:01 20 and I think there were nine cost accounting steps in attaching
21 a zipper to the child's -- to the children's ware. And each
22 of those had been subjected to a cost -- or a time and motion
23 study in order to estimate the cost it would reasonably incur
24 in fulfilling that function.

01:01 25 Q. And how if at all are time and motion studies suited for

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1 measuring skilled professional services?

2 A. They tend not to work very well because they're not
3 repetitive tasks, they differ from engagement to engagement,
4 from function to function, and so they're more difficult to
5 measure in any meaningful way. An observation of what time it
6 took to fulfill a given function in one matter is not
7 necessarily predictive of the effort it will take in another
8 that has different characteristics.

9 Q. And are time and motion studies a required allocation
10 basis?

11 A. No, I don't believe so.

12 Q. Now, Mr. Holder, are you aware that FMG goes through a
13 process of reporting its profitability to the EQAT Board
14 whereby it allocates expenses incurred by its parent AXA
15 Equitable?

16 A. I am aware of that.

17 Q. And, again, just yes or no to this because I want to lay
18 some foundation, have you formed an opinion as to whether it's
19 appropriate for FMG to perform such an allocation?

20 A. I have.

21 Q. What did you do to prepare yourself in forming that
22 opinion?

23 A. Well, as before, I read a large volume of documents,
24 including company documents, Board presentations, the
25 deposition testimony I've alluded to earlier; trial testimony;

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1 I also considered the -- the information gained in my
2 interviews, particularly with Mr. Joenk; those things come to
3 mind.

01:03 4 Q. And what's your opinion as to whether it's appropriate
5 for FMG when reporting its profitability to the EQAT Board, to
6 include costs allocated from its parent AXA Equitable?

7 A. I think that's entirely appropriate. As I indicated
8 earlier the tests for allocability of a cost is its necessity
9 for supporting the function that's being fulfilled. And if
01:03 10 the goal is to determine the full cost of that function, then
11 all of the costs necessarily incurred in support of it would
12 at least in part, through the allocation process, need to be
13 attributed to it.

14 Q. And is it your understanding that AXA Equitable performs
01:03 15 services in support of FMG and the funds?

16 A. That is my understanding.

17 Q. And broadly speaking, what's your -- well, what's that
18 understanding based on?

19 A. Well, again, the same types of activities I've done
01:04 20 before; I've seen, you know, Board packages, I've seen lists
21 of expenses and so on that were incurred, categories of costs
22 that were incurred; I've gained an understanding of the
23 importance of those costs to the appropriate functioning of
24 the -- of the funds, and so on. I've interviewed, again, Mr.
01:04 25 Joenk at some length and on various occasions; read lots of

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1 documents.

2 Q. And broadly speaking, what's your understanding of what
3 some of AXA Equitable's services are to FMG and the funds?

01:04 4 A. Well, AXA Equitable provides a wide range of support
5 services to the funds outside those costs that were charged to
6 FMG. I think it's important to understand that the costs that
7 are being allocated are not limited to just costs that were
8 incurred to support the 50 or 51 employees of FMG. There were
9 certainly some costs that were attributed that support
01:05 10 directly those employees, but many of those costs were
11 supporting the operation of the funds generally.

12 Such things as shareholder activity, the treasury
13 function, accounting function, other functions like that were
14 in part at least necessarily incurred to allow the function --
01:05 15 the funds to function appropriately.

16 Q. Now, Mr. Holder, we've talked about why FMG would
17 allocate costs from its parent AXA Equitable, I'd like to talk
18 now about how the allocations are performed.

19 MR. HORA: Could we hand the witness Defendant's
01:05 20 Exhibit 2050?

21 Q. Do you recognize this document?

22 A. I do.

23 Q. What is it?

24 A. Well, it's an exhibit that I caused to be prepared that
01:06 25 summarizes the processes through with AXA goes in attributing

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1 or allocating costs down to the individual fund allocations.

2 Q. And is this document based on presentations in the EQAT

3 Board materials?

4 A. It is, yes.

01:06

5 Q. Is this document an accurate general representation of

6 the -- I see you cited some source documents in the bottom; is

7 it an accurate general representation of the source documents

8 cited?

9 A. I believe that's the case, yes.

01:06

10 MR. HORA: And your Honor, I'm just using this as an

11 illustrative aid. You've probably seen a different flow chart

12 in the Board materials, we're trying to simplify it a little

13 bit.

14 THE COURT: Okay, thank you.

01:07

15 Q. All right. This is broken out in three steps; correct,

16 Mr. Holder?

17 A. Yes.

18 Q. Could you walk us through what's identified as step A,

19 AXA-CAM?

01:07

20 A. Certainly. Step A begins with AXA Equitable expenses,

21 and those expenses are represented in the general ledger of

22 the trial balance and indeed the financial statements of AXA

23 Equitable. Those costs which are contained in the general

24 ledger are subjected to the audit procedures performed by PwC

01:07

25 in the financial statement audit of AXA's financial

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1 statements. And so I take comfort from that.

2 I think the evidence that I've seen at least is that
3 those are real expenses, their costs that have been incurred,
4 they've been subjected to audit, and I don't understand them
5 at that level to be contested really.

6 But the first step is to allocate those expenses of AXA
7 Equitable generally to the insurance products that AXA
8 Equitable offers. And here, cost drivers are available, as I
9 understand it. There are annual surveys that are sent out to
10 the -- I think they call them business managers, the cost
11 center managers; those individuals report how they spend their
12 time and so on, and what effort goes into various activities.

13 And then there are I think monthly updates sent, and it's
14 based on that data that there is an allocation of the expenses
15 at the corporate-wide level to the several insurance product
16 groups.

17 Q. Okay. And moving on to step B, could you please describe
18 step B of of the methodology?

19 A. Yes. Step B begins with the insurance product group
20 cost, and step B step allocates those insurance product costs
21 into the several elements of the product that each generate
22 revenue. And so, they're allocated to the product wrapper, to
23 the general account and to the investment portfolio. The
24 basis for allocation here is the relative respective revenues
25 generated by each of those three, the product wrapper, the

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1 general account and the investment portfolio.

2 Q. Do you know how step B was developed?

3 A. It was developed as I understand it by FMG, but it was
4 done so in consultation with the professional service firm PwC
5 as well as Ernst & Young. So those two large public
6 accounting or professional service firms were involved in the
7 establishment of this allocation feature.

8 Q. Does the fact that PwC and Ernst & Young were involved in
9 the development of step B, give you any comfort as to the
10 reasonableness of step B?

11 A. It does, yes.

12 Q. And why is that?

13 A. Well, I mean these are very large, among the largest of
14 the professional service firms in the world, in my experience
15 they are very deep repositories of accounting knowledge, and
16 they each have extensive consulting practices; they will have
17 seen many many instances of cost allocations in their
18 practice, and their acceptance or involvement in the creation
19 of this -- this methodology provides some comfort.

20 Q. This is going to be another question where I'm just
21 looking for a yes or no because I do want to lay some
22 foundation. Do you have an opinion as to whether it's
23 appropriate to allocate costs in step B on this basis of
24 relative revenue?

25 A. Yes.

Holder - Direct - Hora

1 Q. All right. Now, what did you look at in coming to that
2 opinion?

3 A. Well, again, I looked at the Board materials that have
4 been alluded to here; I read deposition testimony; looked at
01:11 5 various documents; Excel spreadsheets, and so on; the
6 interviews that I conducted with Mr. Joenk particularly, but
7 Ms. Louie as well, provided information that was useful to me
8 in my analysis; I certainly considered the cost accounting
9 literature of the profession in evaluating the reasonableness
01:11 10 of what's transpiring here.

11 Q. Let's talk a little bit about the cost accounting
12 literature of the profession as you just described it. What
13 exactly are you talking about?

14 A. Well, there are a number of cost accounting treatises and
01:11 15 texts, one that I use particularly in this matter, I think Mr.
16 Barrett alluded to it as well, is a book originally authored
17 by Professor Charles Horngren at Stanford University; that
18 book is I think highly respected, it's certainly widely used
19 in lots of colleges and universities, including our own, my
01:12 20 own.

21 Q. And who is Professor Horngren or who was he?

22 A. Sure. He was an individual that really I think can
23 fairly be said to have kind of pioneered the approach --
24 before the Horngren text, cost accounting was kind of taught
01:12 25 in colleges and universities without too much of a context; it

Holder - Direct - Hora

01:12 1 was let's just try to determine, you know, how much this
 2 particular function costs. But Professor Horngren added to
 3 that the richness of all the management decisions that flow
 4 from that, and how information is designed to be helpful to
 5 those who manage business enterprises. And so the title,
 6 Managerial Approach, I think reveals his really great
 7 contribution to accounting education, to the production of
 8 this textbook.

01:13 9 MR. HORA: Could we the hand the witness what's been
 10 marked as Defendant's Exhibit 1329?

 11 Q. Are you ready?

 12 A. I am, yes, sir.

 13 Q. Do you recognize this, Mr. Holder?

 14 A. I do.

01:13 15 Q. What is it?

 16 A. Well, it's an excerpt from the 13th edition of his
 17 textbook Cost Accounting, an Managerial Emphasis.

 18 Q. And is this textbook something's routinely relied upon by
 19 professionals in the field of cost accounting?

01:14 20 A. In my understanding and view and knowledge it is, yes.

 21 Q. And I think you testified that you reviewed this in
 22 connection with forming your opinions in this matter?

 23 A. I did.

01:14 24 Q. All right. Now, Mr. Holder, how does this Horngren text
 25 inform your opinion with respect to the methodology in step B?

Holder - Direct - Hora

01:14 1 A. Well, the first page beyond the cover page that's
2 provided is page 502, and you can see near the bottom of that
3 page there's a section entitled Criteria to Guide Cost
4 Allocation Decisions. And within that it points out that
5 using activity based costing and related cost drivers, that
6 cause and effect is the primary criterion that's used, and
7 supports the -- the process of using cost drivers.

01:14 8 He also points out that in his view there is a
9 superiority here of cause and effect, and the benefits
10 received criteria --

11 Q. I'm sorry, Mr. Holder, you're on page 5 --

12 A. 502.

13 Q. Okay.

01:15 14 A. In the second paragraph following the criteria. And so
15 he expresses preference for the cause and effect and the
16 benefits received criteria, in the circumstances that he
17 describes, to provide information for economic decisions, yes.

01:15 18 If you look at the four criterion that he lists on the
19 next page, on page 503, he identifies cause and effect and
20 benefits received near the top; and those are followed by two
21 that are not as preferable, fairness or equity and ability to
22 bear the cost allocation. So his preference I think is caught
23 up in the first two that are listed there.

01:16 24 Q. And I'd like you to read if you could the bullet point on
25 benefits received?

Holder - Direct - Hora

01:16 1 A. Very well. It's the second one, 2, it says benefits
2 received: Using this criterion managers identify the
3 beneficiaries of the outputs of the cost object; the costs of
4 the cost object are allocated among the beneficiaries in
5 proportion to the benefits each receives. Consider a
6 corporate-wide advertising program that promotes the general
7 image of the corporation rather than any individual product.
8 The costs of this program may be allocated on the basis of
9 division revenues. The higher the revenues, the higher the
01:16 10 division's allocated cost of the advertising program. The
11 rationale behind this allocation is that divisions with higher
12 revenues apparently benefited from the advertising costs more
13 than divisions with lower revenues, and therefore ought to be
14 allocated more of the advertising costs.

01:16 15 Q. Now, Mr. Holder, what is your ultimate opinion as to
16 whether it's appropriate to allocate costs based on revenues
17 in step B of FMG's cost allocation methodology?

18 A. In my opinion that's appropriate.

19 Q. And why is that?

01:17 20 A. Well, I think there's a probably a combination of cause
21 and effect, as well as benefits received that may exist here.
22 I think the higher revenue item may reveal higher levels of
23 activity; higher levels of activity generally can relate to
24 hire costs being incurred to support that activity. But I
01:17 25 think as or more importantly, using relative revenues here is

Holder - Direct - Hora

1 an example I believe of the benefits received approach; that
2 is, that the higher the revenue, the more benefit from all the
3 supportive activity that's taking place can be reasonably
4 attributed to each of the three revenue producing functions.

01:17

5 Q. Now, Mr. Barrett has testified that step B of FMG's cost
6 allocation methodology is arbitrary, and I think I heard him
7 use the word irrational as well; do you agree with that?

8 A. I do not.

9 Q. Why not?

01:18

10 A. Well, I don't think it's either of those. I certainly
11 understand that in the instant case cost drivers were really
12 not available to make this allocation. Again, if the
13 overarching desire is to estimate the costs that are incurred
14 in generating in this case these revenue streams, that some
15 process of allocation of those costs to those revenue streams
16 is going to be necessary.

01:18

17 And as you can see even in Mr. Horngren's example,
18 using revenue, there -- it's not completely clear in that
19 circumstance that each of those divisions benefited from that
20 general advertising campaign. But it's reasonable to make
21 that assumption, an informed assumption, and to base the
22 allocation of revenue -- or, I'm sorry; of cost on those
23 respective levels of revenue. I find this to be a very
24 similar circumstance.

01:19

01:19

25 Q. Now, are you aware that the net results of FMG's cost

Holder - Direct - Hora

1 allocation methodology is that about \$50 million of AXA

2 Equitable expenses are allocated to FMG for the purposes of

3 reporting its profitability to the EQAT Board?

4 A. I recall that amount, yes.

01:19

5 Q. All right. I'd like to -- I'd like to hand you what's

6 been marked as Plaintiff's Exhibit 273. Do you recognize this

7 document, Mr. Holder?

8 A. I do.

9 Q. What is it?

01:20

10 A. Well, it's been characterized as the Shared Services

11 Agreement between AXA Equitable and FMG.

12 Q. Did you review this agreement in connection with forming

13 your opinions?

14 A. I did.

01:20

15 Q. What is your understanding of what this agreement is?

16 A. Well, it sets out a relationship between FMG and AXA

17 Equitable wherein certain services can be provided, may be

18 provided by AXA Equitable to FMG and for which a charge will

19 be made to FMG.

01:20

20 Q. What's your understanding of how this agreement is used

21 in practice?

22 A. My understanding in practice is that the primary costs

23 that flowed from this particular agreement were related to the

24 50 or so employees that devoted all of their effort to FMG and

01:21

25 by extension the funds that it was managing.

Holder - Direct - Hora

1 Q. And how did you come to that understanding?

2 A. Again, through reading documents, through my interviews
3 with Mr. Joenk and others, reading testimony here in this
4 matter, depositions.

01:21

5 Q. Sure. Now, you're aware that there's a charge that's
6 related to this agreement; right? A charge or an expense that
7 FMG has to pay?

8 A. Yes.

01:21

9 Q. All right. And are you aware that the amount that FMG is
10 charged under this agreement, and let's take 2012, was around
11 \$14 million?

12 A. I have that recollection, yes, sir.

13 Q. And is it your understanding that the \$14 million charge
14 to FMG is included in FMG's audited financial statements?

01:21

15 A. I recall that being the case, yes, sir.

16 Q. Okay. So, my question to you is, how do you reconcile
17 the 49 or roughly \$50 million in allocated expenses from AXA
18 Equitable resulting from FMG's cost allocation methodology,
19 with the roughly \$14 million that's charged to FMG under the

01:22

20 Shared Services Agreement in FMG's audited financial
21 statements?

22 A. I think there's several steps that were incorporated in
23 my analysis. First, in this particular agreement, in
24 paragraph 1 I think it is, it indicates that AXA Equitable

01:22

25 from time to time may provide to FMG, and then there's a long

Holder - Direct - Hora

1 list, the services to be furnished, may include; that speaks
2 to me as an accountant that not all of the costs necessary to
3 the operation of these funds may be provided through the
4 operation of this particular agreement.

01:22 5 As I look at what was -- what were the costs that were
6 charged by AXA Equitable to FMG under this agreement, as I've
7 said my recollection is they primarily related to the
8 compensation cost of these 50 or 51 individuals.

01:23 9 My understanding is further that in order for these
10 funds to operate appropriately, that many many other functions
11 of effort were going to be necessary in addition to those 50
12 or 51 individuals; such things as shareholder distribution
13 activity, when contributions are made, when withdrawals are
14 made, when dividends are paid, the accounting systems and so
01:23 15 on, for keeping up with all of that and doing so accurately
16 and under appropriate control, would not be part of the 50
17 employees, nor would those costs be there to provide human
18 resources type support or travel arrangements to those 50 or
19 51 employees. Those would be services primarily benefitting
01:24 20 the funds directly that were necessary for the funds to
21 operate. There were others such as treasury and various legal
22 costs that would be incurred.

01:24 23 And so, with that knowledge, again, from the work that
24 I had done, you know, and my understanding of the process
25 through which AXA had moved to allocate its general costs to

Holder - Direct - Hora

01:24 1 the various funds, I -- I concluded that the result that was
2 obtained, the 49 or 50 million you alluded to, was reasonable
3 as a result of generally the reasonableness of the process.
4 I'm also aware that amount was about two percent I believe of
5 the total expenses.

01:25 6 And I also evaluated the relationship between the 49
7 million and the 14, and it's clear to me at least that that
8 relationship is not remarkable in any meaningful sense, given
9 the way the companies decided to provide these services and
10 the way they operated.

11 Q. Let's talk about that a little bit, because one of the
12 things that plaintiffs have criticized in the litigation is
13 that the amount of allocated costs, this 49 or 50 million, is
14 a multiple of what's been referred to as FMG's direct costs,
01:25 15 which I think you referred to in a given year 2012 would be 14
16 million; do you think that's a valid criticism?

17 A. No, I don't. I think in order to understand the
18 reasonableness of that relationship one has to understand the
19 way the organization -- AXA was organized, the way it
01:25 20 conducted business, the nature and extent of costs charged,
21 I'll use the word directly to FMG, and the range of costs that
22 would necessarily be incurred in addition to those that would
23 be required for the funds to function appropriately.

24 And there are many instances I think where we judge the
01:26 25 reasonableness, accountants judge the reasonableness of a

Holder - Direct - Hora

1 result through the reasonableness of the process through which
2 one went in arriving at that result.

3 Q. And I just have a couple of more questions for you.

4 Plaintiff's experts in the litigation have calculated 90

01:26

5 percent profit margins for FMG by treating sub-advisory and
6 sub-administrative fees as deductions from revenue, so it's
7 deductions from revenue rather than an expense, and excluding
8 expenses allocated from AXA; do you think that's appropriate?

9 A. Not -- not in my view.

01:26

10 Q. Why not?

11 A. Well, I mean as an isolated statistic it doesn't mean too
12 much for reasons I've already testified about. I think that
13 those sub-advisor and sub-administrative fees very clearly
14 should be reported as expenses not as reductions of revenues.

01:26

15 And again, the test for the allocability of the cost is the
16 necessity, at least in part, of the functions and the services
17 being rendered through the incurrence of those costs are being
18 necessary for the functioning of the funds. If that's the
19 case, some allocation needs to take place.

01:27

20 Q. And what's your opinion about the manner in which FMG
21 calculates its profitability for the EQAT Board?

22 A. It seems reasonable to me, in my view it's a reasonable
23 approach.

24 Q. And why is that?

01:27

25 A. Well, it would be better to look at the --

Holder - Direct - Hora

1 Q. I guess by manner in which FMG calculates its
2 profitability, I meant treating sub-advisory and
3 sub-administrative fees as an expense, and including allocated
4 expenses from AXA and the method by which its done.

01:27

5 A. Well, essentially I think that that better captures the
6 economic realities of what's transpiring here, than reporting
7 them as a reduction of revenue, for all of the reasons we
8 marched through earlier.

9 MR. HORA: One second, your Honor.

01:27

10 (Brief pause.)

11 Q. And Mr. Holder, just one point of classification. You
12 mentioned a little bit earlier in your testimony, I think you
13 said two percent of AXA's expenses were allocated through this
14 allocation methodology process to the funds; could you expand
15 on that a little bit more what you meant by that?

01:28

16 A. Well, it's a rather relatively small amount of the total
17 expenses that were incurred that ultimately get allocated
18 here. I think you have to -- in order to assess
19 reasonableness of amounts you need to place those in an
20 appropriate context, and so that's part of that context.

01:28

21 MR. HORA: Okay. Your Honor, thank you. I don't
22 have any additional questions.

23 THE COURT: All right.

24 MR. HORA: If your Honor does --

01:28

25 THE COURT: All right, thank you.

Holder - Cross - Stevens

1 Cross?

2 MR. STEVENS: Thank you, your Honor.

3 MR. HORA: I need one minute to gather my papers.

4 THE COURT: Do you want to break for 10 minutes and
5 then we'll come back out?

6 MR. HORA: Sure.

7 THE COURT: Mr. Holder, you may step down. We're
8 going to break for 10 minutes, and then we'll be back out for
9 cross.

10 THE WITNESS: Certainly.

11 THE COURT: Okay, thank you.

12 (Recess.)

13 THE COURT: Mr. Holder, you may take the stand.

14 MR. STEVENS: Thank you, your Honor.

15 (CROSS-EXAMINATION OF WILLIAM HOLDER BY MR. STEVENS:)

16 Q. Good afternoon, Dr. Holder.

17 A. Good afternoon.

18 Q. I want to go through a little bit of your background, as
19 it relates to certain issues. Now, you have limited

20 experience in the insurance accounting industry; correct?

21 A. I think that's generally a fair statement. I think
22 that's probably true for any industry there are limitations.

23 Q. Your most robust experience is working with the AcSEC,
24 which we defined before; correct?

25 A. The Accounting Standards Executive Committee, that's

Holder - Cross - Stevens

1 probably not unfair.

2 Q. Okay. And you did so with the AcSEC back in the '70s I
3 believe?

4 A. Pardon me?

01:44 5 Q. In the '70s; correct?

6 A. No, sir. Did you AcSEC?

7 Q. Yes.

8 A. No, that was not in the '70s.

9 Q. When was that?

01:44 10 A. That was '87 through '90 during the savings and loan, or
11 following the crisis.

12 Q. And that was actually only for three years; correct?

13 A. It was for three years, yes, sir.

01:44 14 Q. Okay. And when you were working with them, you developed
15 what you said was an industry guide; is that correct?

16 A. Well, we worked on a number of industry accounting and
17 audit guides, yes.

01:44 18 Q. Okay. And during your deposition you were unable to
19 recall what industry guide you actually worked with and the
20 name of it as it relates to insurance accounting; correct?

21 A. Yes, I'm not sure I would have that recollection today
22 either.

23 Q. Okay. And that's didn't involve mutual fund work;
24 correct?

01:45 25 A. It didn't or did not?

Holder - Cross - Stevens

1 Q. It did not.

2 A. It was an amendment to the investment company's guide as

3 I recall, or there were -- we issued a statement of position

4 that I believe had an effect on a number of industry audit

01:45 5 guides, financial institutions, but including investment

6 companies, yes.

7 Q. But it didn't include any work I'm saying in an

8 investment company or with a mutual fund; correct?

9 A. I don't understand what you mean by that.

01:45 10 Q. You were merely providing guidance pursuant to that

11 industry regulation; correct?

12 A. We were providing accounting standards for mutual funds

13 and investment companies generally.

14 Q. Okay. And some of the experience you talked about

01:45 15 earlier involved some pension accounting that you were

16 involved in; correct?

17 A. Technical accounting?

18 Q. Pension.

19 A. Pension accounting, yes.

01:45 20 Q. And that was some of the government work that you said

21 you consulted on?

22 A. Well, if I recall what you're recalling, I was on the

23 Governmental Accounting Standards Board, and during my time

24 there, we did indeed have a major pension accounting project

01:46 25 and another one very similar to it, other post-employment

Holder - Cross - Stevens

1 benefits, primarily defined healthcare plans, post-retirement
2 healthcare plans.

3 Q. And that's not insurance accounting; correct?

01:46 4 A. I wouldn't know how to respond to that. I mean when
5 you're sponsoring a defined benefit plan, you are providing at
6 least assurances, if not insurance, that will people will
7 receive their pension benefit when they retire. The concepts
8 are very closely related in my mind. There are certainly
9 actuaries involved in calculating benefit obligations and
01:46 10 costs and so on.

11 Q. So, you just indicated the deferred acquisition -- the
12 deferred benefits is pension; correct?

13 A. I think that's one example of a deferred benefit, yes.

01:47 14 Q. Okay. And my question to you is very specific, pension
15 accounting is not insurance accounting; correct?

16 A. There are elements that interact, but there are certainly
17 differences.

01:47 18 MR. STEVENS: Can you approach the witness, Chris,
19 with his deposition testimony, please? Which will be
20 identified as P-852.

21 THE COURT: I didn't hear you, Mr. Stevens.

22 MR. STEVENS: P-852, your Honor.

23 THE COURT: Thank you.

01:47 24 MR. STEVENS: And also P-852.1, which is the
25 exhibits that were attached to his deposition.

Holder - Cross - Stevens

1 MR. KWELTY: Expert report?

2 MR. STEVENS: I'm sorry; the expert report, and then
3 can you also approach with his deposition? Which is marked --
4 what's the marking?

01:48 5 Okay. Can you give the Court a deposition copy
6 also?

7 THE COURT: I don't really need it. You're using it
8 to impeach his credibility?

9 MR. STEVENS: I am, your Honor.

01:48 10 BY MR. STEVENS:

11 Q. I'd like you to turn your attention to page 160 of your
12 deposition testimony.

13 A. I am there.

14 Q. Okay. And actually just before that, I just want you to
01:48 15 look at the first page of your deposition testimony and
16 confirm that what I've given you is in fact the deposition
17 testimony of William H. Holder.

18 A. It's William W. Holder, and that's what the first page
19 says, but yes.

01:48 20 Q. And it's dated November 19, 2014; correct?

21 A. Yes, it says that was well.

22 Q. And do you have a recollection of giving deposition
23 testimony in this case?

24 A. I do.

01:49 25 Q. And did you have the opportunity to review your

Holder - Cross - Stevens

1 deposition testimony prior to today?

2 A. I recall that being the case.

3 Q. And do you have any belief that what's recorded in your
4 deposition testimony isn't a fair and accurate recordation of
5 the testimony you gave on November 19th, 2014?

6 A. I don't have any evidence to the contrary sir, no.

7 Q. Okay. Then with that said I'd like you to turn your
8 attention to page 160. And I'm going to direct your attention
9 to line 3; okay? Are you there?

10 A. I'm there yes, sir.

11 Q. Okay. Line 3 the question was asked: Pension accounting
12 is not insurance accounting, though; you're making an analogy,
13 right; that's correct; question, right?

14 Is that right?

15 A. Yes.

16 Q. And the answer is: I think that's a fair -- fair
17 statement. Correct?

18 A. Yes.

19 Q. And it is true that pension accounting does not involve
20 issues related to deferred acquisition costs also; correct?

21 A. Yes, I don't recall that being the case. There are
22 certainly deferred costs that exist in pension accounting,
23 that are in some ways similar to deferred acquisition costs,
24 but I don't recall deferred acquisition costs being relevant
25 in pension accounting generally.

Holder - Cross - Stevens

1 Q. Okay. And as it relates to deferred costs -- I'm sorry.
2 I'd ask you about deferred acquisition costs and that's fine,
3 and you understand deferred acquisition costs are an element
4 within the industry industry; correct?

01:50

5 A. I have that understanding, yes.

6 Q. And you have that understanding; correct? Meaning -- I'm
7 sorry. And you don't have an expertise in your view in
8 insurance accounting; correct?

01:50

9 A. Well, I have some level of expertise, I'm -- you know,
10 what can I say. Deferred acquisition costs were at least some
11 of the considerations that we made in writing those standards
12 back in '87 through '90, the SOP; I studied the industry then
13 to prepare myself to participate and vote on those standards,
14 but I -- I don't know what you're alluding to really.

01:51

15 Q. Well, is it a fair statement that you feel comfortable
16 with issues involved involved involved in insurance accounting
17 as a general matter?

18 A. Certain aspects of it, yes; others, I haven't
19 familiarized myself in some time.

01:51

20 Q. Okay. And it is a fair statement then that you've never
21 worked within the insurance industry; correct? In other
22 words, for an insurance company?

23 A. I don't recall being the employ of an insurance company,
24 no.

01:51

25 Q. And you never actually addressed or implemented deferred

Holder - Cross - Stevens

1 acquisition costs as it relates to financial accounting for an
2 insurance company; correct?

3 A. I don't recall doing so, no.

4 Q. And you've never worked for an investment company?

01:52 5 A. I don't recall ever being in the employ of an investment
6 company, no.

7 Q. And your experience with investment advisors and/or
8 managers is primarily as an expert witness; correct?

9 A. Could I hear that question again?

01:52 10 Q. Your experience with investment advisors and/or managers
11 is primarily as an expert witness; correct?

12 A. I've run across investment advisors in numerous
13 capacities and circumstances; the sub-advisors here, I think
14 that's the first time I've looked at those relationships.

01:52 15 Q. Okay. And as it relates to cost allocation methodology
16 and the actual implementation of a cost allocation
17 methodology, your main experience was with a Norman, Oklahoma
18 hospital; correct?

19 A. Yes, I think that's a fair statement.

01:53 20 Q. And that was over a period of five years; correct?

21 A. Yes, I was involved in that financial statement audit
22 during a five-year period.

23 Q. Okay. And that was from 1970 to 1975?

24 A. I have that recollection.

01:53 25 Q. All right. And you were retained in this matter to

Holder - Cross - Stevens

1 render certain opinions as it relates to the issues in this
2 case; correct?

3 A. Well, I was retained in the matter to develop opinions in
4 certain areas, yes.

01:53 5 Q. And part of your retention wasn't to render opinions
6 also?

7 A. Well, I don't know what you mean by that. My opinions
8 are mine, they're independent. I was retained to familiarize
9 myself with facts and circumstances and develop opinions,
01:53 10 based on that analysis and that work.

11 Q. And in developing those opinions was it contemplated that
12 you would then have to project those opinions either into a
13 report and/or into court?

14 A. Well, I think there was a tentativeness, I mean I think
01:54 15 it probably -- my inference is at least that it depended on
16 what opinions I developed.

17 Q. Okay. And in doing so you did eventually become engaged
18 by the Milbank firm to render such opinions or to develop such
19 opinions; correct?

01:54 20 A. I was probably retained by the Milbank firm prior to
21 doing work any substantial work, at least in the development
22 of the opinions I'm here expressing today.

23 Q. Okay. And you have before you P-852; correct?

24 A. Yes, yes, I do.

01:54 25 Q. And that's entitled -- or captioned the Holder Report

Holder - Cross - Stevens

1 or -- I'm sorry. That's your report; correct?

2 A. That's the case, yes. It appears to. I see the cover
3 page; I haven't looked through.

4 Q. And you had testified earlier in preparing for this
5 report, a consultation firm by the name of Cornerstone was
6 retained; is that correct?

7 A. I'm sorry, it must be my ears; what kind of firm?

8 Q. Cornerstone?

9 A. No, I heard --

10 Q. Consultation firm?

11 A. Consultation; sorry. Yes, they were retained to assist
12 me at least in part.

13 Q. And had you worked with Cornerstone before?

14 A. I had.

15 Q. And was it your suggestion to retain Cornerstone as it
16 related to the drafting of the Holder Report?

17 A. You know, I honestly don't recall. The -- the exact
18 processes.

19 Q. Okay. And it's true that there's no primary draftsman
20 of the Holder Report; correct?

21 A. Well, the report is mine, the responsibility is mine, I
22 made many of the keystrokes that are contained in the report;
23 I certainly was assisted by Cornerstone research in doing so.
24 I believe the report is mine.

25 Q. And you believe the report is yours because you read it;

Holder - Cross - Stevens

1 correct?

2 A. I certainly -- I have read it, but I certainly don't
3 think that's the exclusive reason that it's mine. I've read a
4 lot of documents, the things that I've alluded to in my direct
5 examination, I conducted interviews with person, I consulted
6 the literature, read deposition testimony.

7 Q. Understood. But I'm just actually talking about
8 specifically as it relates to the report and why you believe
9 it's yours concerning your involvement in the drafting of it.

10 So part of the reason you believe it's yours is because you
11 read it; correct? And you edited it; correct?

12 A. Well, in part those would be I think the reasons, some of
13 the reasons. But certainly not all, nor really substantive
14 ones.

15 Q. And you added verbiage yourself; correct?

16 A. I think that's a fair statement, I made keystrokes
17 myself, I wrote many portions of it initially.

18 Q. And you drafted some of it yourself; correct?

19 A. Yes.

20 Q. Now, you were paid \$750 an hour by the defendants for
21 your work; correct?

22 A. We agreed upon that fee, yes.

23 Q. And were you actually paid by Cornerstone also?

24 A. I do receive compensation from Cornerstone from time to
25 time.

Holder - Cross - Stevens

1 Q. And is that in connection with this litigation?

2 A. I don't know that I would characterize it so precisely, I
3 think -- I don't know the exact algorithm or formula, but
4 Cornerstone does compensate me from time to time, and part of
5 that is based on the level of activity I think that I have
6 with -- with their firm.

7 Q. Okay. And as it relates to the involvement of
8 Cornerstone, there's an individual from Cornerstone who
9 primarily helped you in drafting this report; correct?

10 A. Well, he certainly assisted me in performing the work
11 that was necessary to do -- to prepare the report and develop
12 the opinions.

13 Q. And he actually drafted some of the original report;
14 correct?

15 A. I think he made keystrokes as well, yes.

16 Q. But you had stated earlier in your testimony he drafted
17 as I understand some of it originally; is that a correct
18 statement?

19 A. I -- yeah, that's what I meant by the keystroke.

20 Q. And as it relates to your involvement in the drafting of
21 the report you recall drafting some portions of the rebuttal
22 to Kent Barrett's report; correct?

23 A. I seem to recall that, yes.

24 Q. As well as drafting a portion of the background section;
25 correct?

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1 A. Yes.

2 Q. As well as drafting the discussion of the literature of
3 professional guidance section; correct?

4 A. I believe that to be the case, yes.

01:58 5 Q. Okay. And the drafting of this document occurred in the
6 spring and summer of 2014; is that correct?

7 A. I think that's generally a fair characterization.

8 Q. If I told you that you testified that the drafting was
9 occurring during the spring and summer of this year, which was
01:59 10 2014 during your deposition, do you dispute that?

11 A. No.

12 Q. And it's your belief that you don't believe that Milbank
13 drafted any of the report; correct?

14 A. I don't have a recollection of them. They may have had
01:59 15 some role in the cover page of it, and styling it or
16 something, but I don't recall them drafting or making
17 keystrokes.

18 Q. Okay. And a lot of the interaction with the Milbank firm
19 was done through Mr. Weemes; correct?

01:59 20 A. Yes, we both interacted with the -- with the attorneys,
21 yes, but Mr. Weemes did interact with the attorneys.

22 Q. And as it related to assistance that was provided to you
23 that was provided by Cornerstone; correct?

24 A. Yes -- yes.

01:59 25 Q. As well as Weemes; correct?

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1 A. Well, Mr. Weemes is an employee of Cornerstone.

2 Q. Well, don't you believe that there were a couple other
3 individuals from Cornerstone who assisted Mr. Weemes and
4 yourself in the gathering of documents and drafting of the
5 report?

6 A. I think that's a fair -- fair statement, but Mr. Weemes
7 is not separate and apart from Cornerstone.

8 Q. Okay. And part of what they did was going through a wide
9 range of documents; correct?

10 A. Going through what?

11 Q. A wide range of documents?

12 A. Yes, I think they probably did. I directed them to seek
13 documents from the attorneys from time to time. And they
14 would read them as well as I.

15 Q. And they put together the organizational structure of the
16 report; correct?

17 A. I think they contributed to that, I -- you know,
18 certainly it's my report; if I had objected, and I don't
19 recall you know doing so, sitting here today, but then it
20 would have changed.

21 Q. And you spoke with them, they conveyed information to
22 you; correct?

23 A. Well I did speak with them, they did convey information
24 to me, but most of what I was doing was asking them for
25 documents and to, you know, organize the documents they were

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1 getting in a coherent form, along the lines of the footnotes
2 that are in my report.

3 Q. And part of what you had asked them to do is was provide
4 you with documents that were pertinent to the developing
5 opinions that were emerging from your work; correct?

6 A. I did, I had an abiding instruction to them that any time
7 they saw any documentation, any documents that would be
8 pertinent to the opinions that I was developing, that they
9 were to provide that to me, absolutely.

10 Q. And specific --

11 A. I would want to see those personally.

12 Q. Right. And you specifically told them to direct your
13 attention to areas of deposition that would be of relevance to
14 the developing opinions; correct?

15 A. Absolutely, I read many of the depositions, some of their
16 -- well, there weren't that many. But I did ask them to call
17 my attention, to focus my attention on areas of depositions
18 that in their view would be particularly pertinent,
19 absolutely.

20 Q. Okay. And then after they identified those areas, you
21 then reviewed them; correct?

22 A. Well, I looked at the depositions, but I looked at them
23 more broadly than just those specific areas they identified.

24 Q. Okay. And it's fair to say that Cornerstone actually
25 prepared the documents considered list that's attached to your

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1 expert report; correct?

2 A. I did ask them to keep up with all the documents they
3 were providing -- that they had received from the attorneys
4 and that they were providing to me, yes. That was a good use
5 of their time I thought.

6 Q. Okay. And it's fair to say you didn't read every
7 document on the document list in its entirety; correct?

8 A. I think that's a fair statement, yes.

9 Q. As well as the deposition testimony that was brought to
10 you; correct?

11 A. I think I did read -- there weren't that many
12 depositions, we can certainly look, but I recall reading those
13 -- I mean I read, you know, like at the end of depositions
14 where they have like an index of words that are used and
15 whether -- I didn't read those, I didn't read the front part,
16 but most of the substantive testimony I recall reading.

17 Q. And that was after it was brought to your attention by
18 Cornerstone; correct?

19 A. Pardon me?

20 Q. That was after it was brought to your attention by
21 Cornerstone?

22 A. What was brought to my attention by Cornerstone?

23 Q. The pertinent parts of the relevant parts of the
24 deposition testimony; correct?

25 A. Well, I certainly asked them to be sure and tell me their

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1 view of the pertinent parts of the deposition, but I did not
2 restrict my reading to just those parts.

3 Q. Okay. And there were numerous conversations that you
4 testified to before that occurred between you and Mr. Joenk;
5 correct?

6 A. There were discussions, interviews, yes.

7 Q. And Cornerstone was involved in those discussions;
8 correct?

9 A. I had that general recollection, I think they were at
10 that February meeting, but I don't have a particularly
11 distinct recollection of who was present.

12 Q. And that February meeting would be before or at the
13 beginning of the time period when you were engaged to begin to
14 form your opinions?

15 A. Somewhere thereabouts. It probably followed my actual
16 engagement, but I don't recall the specificity.

17 Q. And Cornerstone actually had conversations with the
18 defendants when you were not present; correct?

19 A. I -- they may have, I don't know that. But I may be
20 forgetting something. I think most of their conversations
21 were with the attorneys that are representing the defendants,
22 but they may have spoken directly with Mr. Joenk, I just don't
23 really recall.

24 Q. And so their discussions with the attorneys then that
25 were representing the defendants, some of those occurred

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1 outside of you; correct?

2 A. Yes, yes, there were many instances in which I would say
3 try to get this information, ask for this information, please
4 try to obtain this information, and they would do so at my
5 direction, yes.

6 Q. Okay. So you relied on Cornerstone to then go to the
7 attorneys to get the information you had requested; correct?

8 A. In those instances where I had asked or directed that
9 they do that, yes.

10 Q. Okay. And you actually asked the attorneys outside of
11 what we had just talked about to provide the pertinent
12 information that they believed would be necessary in
13 developing your opinion; correct?

14 A. Could I hear that question again?

15 Q. Sure.

16 THE COURT: Frank, do you want to restate it?

17 (Question read back by the reporter.)

18 THE WITNESS: I don't understand the phrase in the
19 question.

20 THE COURT: Restate your question, Mr. Stevens.

21 MR. STEVENS: Yes, your Honor.

22 BY MR. STEVENS:

23 Q. You also asked the attorneys to provide Cornerstone with
24 all of the information that would be pertinent to developing
25 your opinion; correct?

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1 A. Yes, all of the information that was available, yes, I
2 would have done that.

3 Q. Okay. And part of the documents that you asked
4 Cornerstone to look into was you wanted a pretty thorough
5 search of professional literature; correct?

6 A. Yes, I asked them to contribute their ideas as to the
7 relevant portions of the literature that would be informative
8 in forming my opinions.

9 Q. Right. And you did so in order to immediately understand
10 the concepts and guidance for cost accounting; correct?

11 A. Well, I think I had an understanding of those concepts
12 and the guidance that were contained in there. Generally when
13 you embark on an engagement like this there's a degree of
14 specificity and support that at least I like to generate and
15 be able to refer to. So while I felt comfortable with the
16 contents of Professor Horngren's book, for example, I would
17 want to get it, refresh my recollection and I would want to
18 cite to it and to other literature of the profession, and
19 refresh my recollection. And yes, I did ask them to get that
20 literature, to assemble it and to provide to it me, rather
21 than getting it myself; that's typically how I would use a
22 research assistant.

23 Q. Okay.

24 A. And was really no different here.

25 Q. And some of the guidance that you sought from Cornerstone

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1 or from others was a book by the name of Fund Governance,
2 Legal Duties of Investment Company Directors book; correct?
3 A. I recall seeing that and reading it and becoming familiar
4 with it, yes.

02:07

5 Q. Okay. And did you read that book in its entirety?

6 A. I don't recall doing so. I would need to see the book at
7 this point and -- you know, I think I probably footnoted just
8 those portions of it that were of particular relevance to the
9 opinions I was being asked to develop.

02:07

10 Q. Okay. And as it relates to that book, you had never
11 consulted that book prior to this litigation; correct?

12 A. I don't recall doing so.

13 Q. Okay. And you're aware that the author of the book is an
14 attorney; correct?

02:08

15 A. I do have that recollection.

16 Q. Okay. And do you also recall that you were unable to
17 testify during a deposition of who selected the quotes during
18 the Fund Governance book that was contained within your
19 deposition?

02:08

20 A. I don't -- I don't recall that. I would have been aware
21 that they were there. I recall looking at the book, but I
22 don't recall who may have identified the specific elements
23 that I chose to include in the report.

02:08

24 Q. And you have P-852 before you, correct, your expert
25 report?

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1 A. Yes, sir, I still do.

2 Q. I want you to turn your attention to page 11 of your
3 report.

4 A. I'm there.

02:08 5 Q. Specifically paragraph 25.

6 A. I'm there.

7 Q. And this paragraph 25 discusses that AXA maintains FMG's
8 bank accounts; correct?

9 (Witness reviewing.)

02:09 10 A. I see that phrase in the paragraph, yes.

11 Q. And you don't have a recollection as to whether or not
12 you drafted this section of the report; correct?

13 A. You know, sitting here today I probably don't have a
14 specific recollection of which specific parts I individually
02:09 15 and originally authored in general, but there were many that I
16 did. I don't recall who might have put pen to paper with the
17 first draft of what's in paragraph 25. I can tell you that I
18 did read Mr. Joenk's deposition, and at least at one time was
19 aware of this list of things that is -- that is identified
02:10 20 here.

21 Q. Okay. And if Mr. Joenk was wrong as to any of this
22 things identified in that paragraph, would that change your
23 opinion in this case?

24 A. Not necessarily. I mean this seems -- no, it would not;
02:10 25 at least not necessarily.

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1 Q. And as it relates to -- you indicated as you sit here
2 today you don't have a recollection as to what parts of this
3 report you drafted in 2014 when you gave your deposition that
4 was in November; correct?

02:10 5 A. I recall that being the case, yes.

6 Q. And you indicated that this report was being drafted from
7 the spring to the summer; correct?

8 A. I recall that.

9 Q. Okay. So that was roughly two to three months -- the
02:10 10 deposition was roughly two to three months after the final
11 draft of this report was done; correct?

12 A. Little over three months I guess.

13 Q. Okay. And actually your report's dated August 8th, 2014;
14 correct?

02:11 15 A. It is, yes.

16 Q. And in 2014 as relates to paragraph 25, you didn't have a
17 recollection as to whether or not you drafted that report even
18 back then -- or that paragraph even back then; correct?

19 A. I don't recall, I may or may not have; we have to look at
02:11 20 my deposition testimony.

21 Q. I'd like you then turn to page 96 of your deposition
22 testimony, please.

23 A. Sure. I'm there.

24 Q. Okay. If you go to -- we'll start with line 1. The
02:11 25 question is: In your report on page 11, I guess it's

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1 paragraph 25, you did say that -- and it says you referred to
2 that AXA maintains FMG's bank accounts.

3 Do you see that?

4 A. I do.

02:11 5 Q. And the answer is: Um-hmm. The question: So does that
6 mean that FMG has its own bank accounts? The answer is: No,
7 I don't think so, I mean that doesn't necessarily imply that.

8 Correct?

9 A. That's what I said then, yes.

02:12 10 Q. So the follow-up question was: Did you write that? And
11 your answer was: I don't recall if I drafted these actual
12 words or not, I certainly read it, I approved it, I adopted it
13 as mine.

14 Correct?

02:12 15 A. That's what the transcript says, yes.

16 Q. Okay. So then back in 2014, three months after you
17 drafted this report, you then were unsure as to whether or not
18 you drafted that specific paragraph in the report; correct?

02:12 19 A. Well, you know, it's a little unclear what you're
20 alluding to here, whether it's confined to just the bank
21 account reference or the entirety of paragraph 25. But it is
22 what it is. I mean I don't have a better recollection today
23 than I did then.

02:12 24 Q. Okay. And you're paid as we indicated by the defendants;
25 correct?

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1 A. I'm paid by what?

2 Q. By the defendant for your work on this report; correct?

3 A. That's my general understanding, yes.

4 Q. And in order to get paid you have to submit something to
5 the defendants; correct?

6 A. I submit monthly invoices with a summary of the time that
7 I've spent, yes.

8 Q. Okay. And are those invoices in your view trustworthy?

9 A. Well, they may contain errors, but I certainly intend
10 them to be accurate.

11 Q. Okay. And based on the invoices you submitted, were you
12 actually paid by the defendant for the work contained within
13 those invoices?

14 A. I don't think I've been paid for some of the most recent
15 ones, but generally, yes.

16 Q. Okay. Well, as it related to the work you performed in
17 2014, were you paid for that work?

18 A. Yes, I have that recollection.

19 MR. STEVENS: Chris, could you hand the witness and
20 the judge P-849 for identification purposes?

21 Q. Do you recognize that document, Dr. Holder?

22 A. Yes, it would appear to be the invoice I alluded -- the
23 type of invoice I alluded to earlier for the month of July.

24 Q. Okay. And as you're reviewing that invoice does it
25 appear to be trustworthy?

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1 A. I don't know what you mean by trustworthy. I don't have
2 any indication or recollection that it contains errors.

3 Q. So, is it a fair and accurate representation then of the
4 invoice you submitted back in July -- or for the July work you
5 did from July 1st to July 9th?

6 A. I don't have much of a recollection independent of what
7 I'm looking at here.

8 Q. I understand that.

9 A. At this time, but it --

10 Q. What I'm saying, though, is that invoice -- does that
11 appear to be a fair and accurate representation of the invoice
12 you submitted to the defendants for payment?

13 A. As far as I know, yes.

14 Q. And I want to direct your attention to July 1st of that
15 year. Do you see that?

16 A. I do.

17 Q. And on that it indicates that you continue to draft a
18 report?

19 A. Yes.

20 Q. Is that the first time that you began to draft a report
21 as it related to this case?

22 A. I -- I doubt that. I certainly -- you can see here that
23 I was rendering services prior to the July period; I don't
24 know how I might have characterized those services previously.

25 But I -- if I recall correctly the drafting of the report

Holder - Cross - Stevens

1 began earlier and I would have been involved in that drafting.

2 Q. Okay. And that would be -- and if you were involved in

3 that drafting earlier, there would be an invoice that said

4 drafted report; correct?

02:16 5 A. Not necessarily, no.

6 Q. So you wouldn't have billed for the drafting of any of

7 the report prior to July 1st, 2014?

8 A. I may not have characterized it that way, there are

9 different ways to characterize things.

02:16 10 Q. Well, I'm going to have then P-856 shown to you, please.

11 (Brief pause.)

12 MR. STEVENS: Let's go to P-847. How's that.

13 Q. Do you recognize what's been handed to you as P-847?

14 A. I do.

02:17 15 Q. And that's dated June 6th, 2014; correct?

16 A. It is.

17 Q. And that's a statement of services for May of 2014;

18 correct?

19 A. Yes.

02:17 20 Q. And there's no entries in that May of 2014 document that

21 indicates anything concerning drafting of a report; correct?

22 A. I don't see the word drafting in the items that are

23 identified there.

24 Q. Okay.

02:18 25 MR. STEVENS: And I'd like 848 to be given to the

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1 witness, please.

2 Q. And P-848 is a document at the front, that's dated July
3 7th, 2014; correct?

4 A. It is, yes.

02:18 5 Q. And it indicates that it's a statement for services for
6 the month of June 2014; correct?

7 A. Yes.

8 Q. And if you look on page 2, it has a listing of services;
9 correct?

02:18 10 A. I'm sorry; say again?

11 Q. It has a listing of services on page 2?

12 A. Yes.

13 Q. And again, there's no indication of the drafting of a
14 report at all; correct?

02:19 15 A. I don't see the word drafting there either.

16 Q. Do you see the word writing a report?

17 A. I do not.

18 Q. Okay.

02:19 19 MR. STEVENS: Your Honor, at this point plaintiffs
20 would seek to admit P-847, 848 and 849 into evidence.

21 MR. HORA: No objection.

22 THE COURT: No objection, all right. Admitted.

23 MR. STEVENS: Thank you?

24 THE COURT: So, 847; what was the other one, 849?

02:19 25 MR. STEVENS: I'm sorry, your Honor?

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1 THE COURT: I'm trying to figure out -- you had
2 three documents you wanted admitted, 849, 847 and?

3 MR. STEVENS: And 848.

4 THE COURT: Okay. Admitted.

02:19 5 (Plaintiff's Exhibits 847, 848, 849 were marked into
6 evidence.)

7 BY MR. STEVENS:

8 Q. And as it relate now to your Norman, Oklahoma experience
9 and your prior work experience, there was never a time that
02:20 10 you recalled where you ever used revenues as a basis to
11 allocate expenses; correct?

12 A. As I recall testifying that's generally the case. There
13 was the purchasing department in the hospital, they didn't
14 prepare a separate financial statement for purchasing, but had
02:20 15 they, that allocation would probably have been based on
16 revenues. But that's the extent of my recollection sitting
17 here.

18 Q. Okay. But that didn't occur you said?

19 A. What didn't occur was the separate financial statements
02:20 20 were not prepared for the purchasing department.

21 Q. And you never suggested in any of your written
22 illustrations to use revenue to drive an expense allocation;
23 correct?

24 A. You know, I honestly don't recall, I'd have to look back.
02:21 25 There were several articles, there's the manuscript on cost

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1 allocation, I think we've discussed it, but when California
2 passed a law that required not charging more for government
3 services than the cost of providing those services, I was
4 commissioned along with a co-author to write a manual, so that
5 cities could do a cost allocation and make a reasonable
6 determination of the cost of fulfilling various functions they
7 charged for, like marriage licenses and so on for that
8 purpose. Whether revenue was the basis for allocation, I mean
9 I just don't recall.

10 Q. The answer is you don't recall ever suggesting that.

11 A. Yes, I think that's a fair -- fair statement. Other
12 than, you know, Professor Horngren's use of revenue as an
13 example and the work that I've done in this particular case.

14 Q. Okay, understood. And as it related to Norman cost
15 allocation which is a hospital, you didn't -- you used various
16 bases to allocate the revenue produced in the areas; correct?

17 A. Could I hear that again?

18 Q. As related to the Norman cost allocation which was a
19 hospital that you had discussed working on for five years --
20 correct?

21 A. Yes.

22 Q. You used various bases to allocate to the revenue
23 producing areas --

24 A. Yes, that's a true statement.

25 Q. Cause and effect to the producing areas; correct?

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1 A. No, I don't think you can attribute that degree of
2 causation.

3 Q. Okay.

4 A. To many of the allocation bases that are used.

02:22 5 Q. But you were able to determine cost drivers for the
6 allocation process; correct?

7 A. Certainly not in all circumstances.

8 Q. But you didn't just allocate pursuant to the portion of
9 revenue as you testified to before; correct?

02:22 10 A. Like I testified before?

11 Q. Correct. You said that the only time -- the only
12 possibility you thought of allocating pursuant to revenue
13 would have been within that one department that you ended up
14 not doing it; correct?

02:23 15 A. Sure, we're communicating, sure.

16 Q. Okay, good. I appreciate that. And each year as related
17 to the Norman -- the five years that you were involved in the
18 cost allocation methodology, there was considerable effort
19 made to put together a cost allocation methodology per year;
02:23 20 correct?

21 A. Well, yes, I mean they varied if I recall correctly from
22 year to year, but in the method at some level remained the
23 same; it was a step down cost, function rather than
24 simultaneous equations or something like that.

02:23 25 Q. But because they varied, it's fair to say that in each of

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1 those years there would be considerable effort made to put
2 together a cost allocation process; correct?

3 A. I think that's a fair characterization of our work, yes.

4 Q. And that's fair as it relates to cost allocation;
5 correct?

6 A. What's fair as it relates to cost allocation?

7 Q. That each year there should be considerable effort put in
8 to the cost allocation to develop -- or to review the cost
9 allocation process; correct?

10 A. No, I don't think so.

11 Q. But you did that in the Norman, Oklahoma case; right?

12 A. Yes, as I had indicated the Medicare formula had just
13 been put in place and there were changes being made to the
14 that -- to those regulations and so on, and so we did try to
15 stay abreast of the regulations and what they called for and
16 required, and that would have an effect on the cost allocation
17 process as used or at least it could have.

18 Q. And that was based on your intent to be diligent as it
19 related to the appropriate allocation of the costs to the
20 appropriate revenue producing areas; correct?

21 A. I need to hear the very first part of that sentence
22 again; you spoke so quickly. I apologize, sir.

23 Q. You know what, don't worry about it; I'll move on.

24 Now, as it relates to the need for FMG to use the

25 AXA-CAM, in your deposition you're unable to point to one

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1 specific document that you were able to identify that told you
2 that this was necessary; correct?

3 A. That told me what was necessary?

4 Q. The need to allocate -- that FMG need to allocate
5 pursuant to the FMG-CAM.

6 A. I think that's the process that they developed.

7 Q. Correct. But you don't have any specific document that
8 you can point to that shows that there's a need to allocate
9 additional expenses to FMG; correct?

10 A. And you're asking me at the time that I gave my
11 deposition?

12 Q. Correct.

13 A. You know, I just don't recall.

14 Q. Okay.

15 A. I recall -- you know, I've refreshed my recollection to
16 prepare myself for trial today. I'm aware of the range of
17 costs, that it certainly resonates with me that those kinds of
18 costs would be necessary for the funds to operate
19 appropriately, and that thus some allocation would be an
20 appropriate approach to determine the full cost of providing
21 the service, providing the function.

22 Q. And really the main area that you were able to identify,
23 at least in your deposition, was what's attached to -- is
24 P-8521, which is your documents supplied or your exhibits, and
25 it was specifically exhibit 6, page 15.

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1 A. I'm sorry; I'm trying to find the sixth exhibit.

2 Q. If you go to then -- if you go to your documents, go to

3 your exhibits, go to page 45 of 157, which is exhibit --

4 A. Sure, that's helpful.

02:27 5 Q. -- 6.

6 A. Yeah, I'm there.

7 Q. Okay. And you recognize that document; correct?

8 A. I do, yes, sir.

9 Q. And that's the expense allocation document that reflects

02:27 10 the cost allocation methodology used by FMG; correct?

11 MR. HORA: Mr. Stevens, if I can just see what

12 you're referring to? Okay. I have it.

13 A. In summary form, yes. I think that's a fair

14 characterization.

02:27 15 Q. And this is one of the documents that you reviewed when

16 rendering your decision; correct?

17 A. This is one of the documents that was available to me,

18 yes.

19 Q. And that's one of the documents that in your view speaks

02:27 20 to the need to allocate if you want to determine the full cost

21 of rendering services to the funds; correct?

22 A. No, I think this is more of a description of the

23 allocation process.

24 Q. Okay. And so then at your deposition testimony when you

02:28 25 stated that, you meant to state that as really just a

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1 description of what occurred; correct?

2 A. Well, it's certainly not this disconsonant with my
3 understanding of the kinds of costs that are necessary to
4 support these activities, but I -- I believe sitting here
5 today that this is best characterized as a description of the
6 cost allocation at a summary level.

7 THE COURT: So, Mr. Stevens, can we break for lunch
8 at the present time?

9 MR. STEVENS: Absolutely.

10 THE COURT: Okay. So we'll break at the present
11 time, we'll reconvene at 2 o'clock.

12 So just so I have the timing down, we agreed
13 yesterday afternoon that the defendants would have the same
14 amount of time for cross-examination as the plaintiffs used
15 for direct. So, on Mr. Holder, I started this morning, I
16 believe it was at 10:50 and they went to -- I have 12:27; so
17 it's about an hour and 40 minutes I believe. And so you
18 started at 12:38, and now it's 1:22; so you've gone about 44
19 minutes.

20 MR. STEVENS: Sound good, Judge.

21 THE COURT: So you have another hour or so.

22 MR. STEVENS: All right. Thank you, your Honor.

23 THE COURT: If I didn't tell the time right and --

24 MR. MURPHY: I could shade it.

25 MR. HORA: We're not going to nitpick a couple

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1 minutes.

2 THE COURT: Okay. So thank you. I'll be back at
3 2:00.

4 Mr. Holder, you may step down.

02:29 5 (Luncheon recess.)

6 THE COURT: Good afternoon. Please be seated.

7 Are you ready, Mr. Stevens?

8 MR. STEVENS: I am, your Honor. Thank you.

9 THE COURT: Mr. Holder, could you take the stand?

03:26 10 So, you're still under oath, sir.

11 THE WITNESS: Yes, sir.

12 THE COURT: Mr. Stevens?

13 MR. STEVENS: Thank you, your Honor.

14 BY MR. STEVENS:

03:26 15 Q. Dr. Holder, as it related to how you learned the cost
16 allocation methodology employed by FMG, you were able to learn
17 it by having discussions with individuals such as Mr. Joenk;
18 correct?

19 A. That be would part of it, yes.

03:26 20 Q. Ms. Louie; correct?

21 A. Yes.

22 Q. A couple other individuals from FMG; correct?

23 A. Yes.

24 Q. You never had any conversations with anyone from

03:26 25 PricewaterhouseCoopers, did you?

Holder - Cross - Stevens

1 A. Not about this matter, no.

2 Q. Or JP Morgan?

3 A. Not about this matter, as I recall, no.

4 Q. Or Ernst & Young?

03:26 5 A. Not about this matter.

6 Q. Okay. And you had testified before as related to step A
7 of the AXA-CAM; do you recall that testimony?

8 A. Yes.

03:27 9 MR. STEVENS: And it may help if I have what's
10 already been marked into evidence I believe -- P-210 given to
11 the witness and also to the Court?

12 Q. Do you recognize this document, Mr. Holder?

13 A. I do.

03:27 14 Q. And this is actually the document that's contained as
15 Exhibit 6 to your expert report; correct?

16 A. I -- I could look and verify that; I recall this being
17 that exhibit, yes.

18 Q. Okay. So you do recollect that this is in your expert
19 report; correct?

03:27 20 A. Yes, I do.

21 Q. So if there's any deposition testimony as it relates to
22 Exhibit 6, it would be referring to this document; correct?

03:28 23 A. Again, I haven't looked at this document. I don't know,
24 it may contain pages that aren't in the exhibit, I haven't
25 compared them sitting here, but I'll accept your

Holder - Cross - Stevens

1 representation that that's the case.

2 Q. That's fine. If we have to we can go through that

3 process; okay?

4 A. Sure.

03:28 5 Q. I'd like to direct your attention then to page 2 of this
6 document; do you see that?

7 A. I am there, yes.

8 Q. And it's entitled Expense Allocation and Methodology;

9 correct?

03:28 10 A. Yes.

11 Q. And it's an EQAT Board update; correct?

12 A. Yes.

13 Q. And is it your understanding that this document was
14 presented to the EQAT Board?

03:28 15 A. I have that general understanding.

16 Q. And so what I'd like to do then is just direct your
17 attention to what is page 15 of that document, and it's Bate
18 stamp 6745 which is at the bottom right.

19 A. I'm there, yes.

03:28 20 Q. And if you look at the column to the left where it says
21 A, is that fair to say that's the AXA-CAM?

22 A. Yes, I've heard it characterized that way, I certainly
23 accept it.

03:29 24 Q. And you then as it related to the document we had before
25 the Court, which is P-2050, which was your cost allocation

Holder - Cross - Stevens

1 methodology overview, reflected what's in step A on that
2 document; correct?

3 A. I think it's -- the page with Bates number ending 6745 is
4 a summary of these processes; mine is essentially a summary of
5 this summary.

6 Q. Okay.

7 A. But yes.

8 Q. Understood. And so, as it relates to step A, isn't it
9 true that the AXA-CAM is able to actually allocate costs in
10 step A; correct?

11 A. That's -- that's my general understanding, yes.

12 Q. And that results then in the allocation of the expenses
13 to the various products; correct?

14 A. I have that understanding, yes.

15 Q. And that AXA's able to allocate those expenses to the
16 products based on cost drivers that are identified by business
17 owners; correct?

18 A. Generally, that's my understanding.

19 Q. And they also use surveys with the managers and business
20 owners of those products; correct?

21 A. My understanding that's part of the identification of the
22 cost drivers and the various allocations, but yes.

23 Q. And that's all done by AXA as it relates to the total AXA
24 expenses; correct?

25 A. Well, you see the adjustments to total AXA expenses here,

Holder - Cross - Stevens

1 I mean there are --

2 Q. Understood.

3 A. I'm sorry?

4 Q. Understood; we can get to that. I just wanted to

03:30 5 establish that that process is in relation to the total AXA
6 expenses; correct?

7 A. Well, my understanding is that some of the AXA expenses

8 are charged directly to FMG, and then you have the deferred

9 acquisition costs, actuarial adjustment, but having said that

03:30 10 I -- I don't take further exception to agreeing with
11 your assertion.

12 Q. Okay. As it relates to those surveys that they

13 performed, based on those surveys adjustments are made each

14 year to the cost drivers; correct?

03:31 15 A. If they are found to be appropriate, yes. Based on that
16 process.

17 Q. And that's a similar process that you -- or that you

18 actually engaged in as it related to the Norman, Oklahoma cost

19 allocation methodology that you employed from 1970 to 1975;

03:31 20 correct?

21 A. It's similar.

22 Q. Process where it was reviewed every year?

23 A. No.

24 Q. You didn't review the cost allocation methodology every

03:31 25 year when you were working with Norman, Oklahoma?

Holder - Cross - Stevens

1 A. We did that, but we didn't do so in the same manner as
2 it's done here. I don't recall surveys being sent annually
3 and monthly kind of updates and so on. But --

4 Q. I'm sorry; it may have been a bad question on my behalf.
5 I didn't mean actually as it related to surveys, I just meant
6 that based on variables as it related to what was discovered
7 each year, adjustments were made by AXA; correct?

8 A. As it relates to this part A, I think that's the case
9 insofar as changes were made.

10 Q. Right. And what I had meant to say that's the same
11 process as related to the adjustments that you engaged in in
12 Norman, Oklahoma depending on what variables arose each year;
13 correct?

14 A. No, I don't think so. The changes we would make in the
15 hospital that we -- that I've been answering questions about,
16 many of those, perhaps most were propelled by changes in the
17 Medicare regulations. As I recall they were changing, you
18 know, rather quickly as Medicare was rather a new program
19 then. And in addition to that it would be -- things were
20 fairly stable in a number of the revenue generating
21 activities, although there were advancements being made --
22 it's just so long ago I've forgotten, but it was in responses
23 to changes, and they weren't just changed every year in the
24 face of a stable environment.

25 Q. But they were adjusted if there was a change was all I

Holder - Cross - Stevens

1 was asking --

2 A. When there are changes in the regulatory environment, or
3 when there were changes in the basic structures of operations,
4 yes.

03:33 5 Q. And as it relates to the cost allocation methodology that
6 was used by FMG, you are not prepared to say how it is that
7 FMG should have actually allocated any expenses down to the
8 EQAT; correct?

03:33 9 A. I don't completely understand that question; the process
10 that we've just been --

11 THE COURT: If you don't understand -- you have to
12 rephrase.

13 MR. STEVENS: I'll rephrase, Judge. Okay.

14 BY MR. STEVENS:

03:33 15 Q. So you're not able to -- or you're not willing to
16 personally say how you would allocate any expenses if they
17 should have been allocated pursuant to expenses down -- let me
18 rephrase.

19 THE COURT: So you're starting over?

03:34 20 MR. STEVENS: I am. Because I got little flustered.

21 Q. Assuming that expenses needed to be further allocated
22 outside of what has already been charged to FMG by AXA
23 pursuant to the Shared Services Agreement, you are not willing
24 to offer a personal opinion as to how you would do that;
03:34 25 correct?

Holder - Cross - Stevens

1 MR. HORA: Objection; confusing.

2 THE COURT: Well, do you understand the question,

3 Mr. Holder?

4 THE WITNESS: I don't understand the personal
5 opinion particularly --

6 THE COURT: Then you have to rephrase.

7 THE WITNESS: -- well.

8 BY MR. STEVENS:

9 Q. It was your task as it related to your hiring and your
10 judging or your review of the cost allocation methodology in
11 this case, was merely to assess the reasonableness of the
12 allocation method being used; correct?

13 A. I think that's generally a fair characterization in the
14 three phases.

15 Q. Okay. And it was not your intent to try to develop a
16 cost allocation methodology that would be different than what
17 was used in the cost allocation methodology by FMG; correct?

18 A. I think that's a fair statement, yes.

19 Q. And you did not consider alternatives to the revenue
20 based allocation system used by FMG in this matter; correct?

21 A. Your question's now focusing on part B or the element B
22 of the allocation?

23 Q. I should back that up. It's my understand and from your
24 deposition testimony that you understood that the FMG cost

25 allocation methodology was step B and C of what's contained on

Holder - Cross - Stevens

1 page 15 of P-210; is that correct?

2 A. I heard it characterized that way, I'm comfortable with
3 that, yes.

4 Q. Well, in Defendant's Exhibit 2050 you actually put step B
5 as FMG-CAM; right?

6 A. Yes.

7 Q. So then you're familiar with that; correct?

8 A. Yes.

9 Q. Step A is the AXA-CAM; correct?

10 A. That's the way they've been characterized generally, I've
11 adopted those characterizations myself, sure.

12 Q. And we discussed the various manners in which the AXA-CAM
13 allocates the cost as it relates to surveys and questioning of
14 businesses and managers; right?

15 A. We have, yes.

16 Q. And that they were able to identify cost drivers based on
17 that; correct?

18 A. They were -- yes, they were able to -- they may have
19 identified cost drivers and then used this mechanism to

20 measure the extent to which each one would be considered a
21 cost driver for purposes of this specific allocation.

22 Q. Right. And as related then to step B and C, the FMG-CAM,
23 you didn't do any independent investigation to determine
24 whether or not there were cost drivers available to allocate
25 expenses down to the products if necessary; correct?

Holder - Cross - Stevens

1 A. In the work I performed I didn't identify what I would
2 consider to be available cost drivers.

3 Q. And you didn't try to identify available cost drivers;
4 correct?

03:37 5 A. That wasn't the focus of my work. But I can say that
6 none came to my attention that I recognized at least.

7 Q. And I'd like to direct your attention to paragraph 48 of
8 your expert report. Do you have that still before you, sir?

9 A. I am getting there.

03:37 10 Q. Okay, thanks. And that's Plaintiff's Exhibit 852.

11 A. It is, and I have paragraph 48 in front of me.

12 Q. Okay, thank you. And I'd like to direct your attention
13 to the paragraph that you indicate, many of the allocated
14 expenses arise --

03:37 15 A. I'm sorry, forgive me; is it the first many down in the
16 middle of the paragraph?

17 Q. Yes, where it says --

18 A. I'm with you --

19 Q. Many of the allocated expenses?

03:37 20 A. Yes.

21 Q. Okay. It says: Many of the allocated expenses arise
22 because of revenue producing activities, such as sales
23 activities engaged by AXA Equitable. Correct?

24 A. Yes, it says that.

03:38 25 Q. And you go on further to state: It is noteworthy that

Holder - Cross - Stevens

1 almost half of the 2.275 billion in AXA Equitable allocated
2 expenses in 2012 pertain to commission and acquisition related
3 expenses; correct?

4 A. Yes, they're words to that general effect here.

03:38

5 Q. Okay. And then you continue: The relationship between
6 sales related compensation and revenues, is clearly consistent
7 with the cause and effect criterion supported in the cost
8 accounting literature. Correct?

9 A. That -- those words are there, yes.

03:38

10 Q. Okay. And are those correct statements that are
11 contained within your report?

12 A. I'm not aware that they're inaccurate. I -- I believe
13 them to be a reasonable characterization of facts,
14 circumstances and judgment.

03:39

15 Q. Okay. Do you recall if you actually drafted this
16 section?

17 A. No, I don't recall here. I can tell you that I worked on
18 this section, I almost certainly made keystrokes to all of the
19 sections in here, but I can't recall who might have been the
20 original drafter of what became this paragraph.

03:39

21 Q. Okay. And basically what that paragraph is saying that
22 is sales commissions have a correlation with revenues as it
23 relates to the products; correct?

24 A. I did not -- I think it indicates there's a relationship;
25 I did not try to measure correlation, that's essentially a

03:39

Holder - Cross - Stevens

1 statistical term, I did not attempt to develop correlation
2 coefficients.

3 Q. But then as related to your opinion as to the
4 reasonableness of the cost allocation methodology, you
03:40 5 indicated in this paragraph that part of the reason for the
6 reasonableness is that these sales commissions and sales
7 related activities have a relationship then to the revenue
8 aspect of the EQAT; correct?

9 A. If I understand your question I think generally that's
03:40 10 the case, yes.

11 Q. And by sales related compensation are you referring to
12 commissions and other compensation that AXA Equitable pays to
13 its insurance product sales force and sales agents?

14 A. Let me look at the context if I may for a moment.

03:40 15 Well, these are revenues -- the basis for the
16 allocation is generally revenues generated from the investors
17 or shareholders or participants.

18 Q. Okay. And so as it relates to the sales related
19 compensation that you're discussing, are you -- have you ever
03:41 20 heard the term distribution expenses?

21 A. Yes.

22 Q. Okay. Would you consider those to be distribution
23 expenses?

24 A. Would I consider -- what's those?

03:41 25 Q. The sales related compensation that you reference in

Holder - Cross - Stevens

1 paragraph 48 of your report.

2 A. They may well be among them, yes; I don't recall

3 specifically sitting here.

4 Q. Okay. Is that something that you would have known when

03:41 5 you drafted your report?

6 A. I think I would have known it at one time given its

7 presence here, I don't recall beyond that, though.

8 Q. Okay. And if I could turn your attention the Defendant's

9 Exhibit 1329, which you should have before you from your

03:41 10 testimony earlier this morning.

11 A. The cost accounting book?

12 Q. Correct.

13 A. I have that in front of me.

14 Q. Okay. I want to just direct your attention to footnote 2

03:42 15 on page -- what's the second page of this document; correct?

16 Do you see that?

17 A. Almost. I'm there.

18 Q. Okay. And it talks about the Federal Accounting

19 Standards Advisory Board; are you familiar with that?

03:42 20 A. I am familiar with that organization.

21 Q. And it indicates that cost assignments should be

22 performed either, A, directly tracing costs whenever feasible

23 and economically practicable -- correct?

24 A. I see that, yes.

03:42 25 Q. And B, assigning costs on a cause and effect basis --

Holder - Cross - Stevens

1 correct?

2 A. Yes.

3 Q. And C, allocating costs on a reasonable and consistent
4 basis. Right?

03:42 5 A. I see what you've read, yes.

6 Q. And then you had referenced on the next page the benefits
7 received criterion listed in this; correct?

8 A. Yes.

9 Q. And in that benefits received criterion, the example they
10 give to consider corporate-wide advertising program; right?

11 A. Yes, that's the example that professor included in -- in
12 that -- in part B -- or part 2; I'm sorry, yes, Professor
13 Horngren included.

14 Q. Right. And so the benefit -- or the comparison as it
15 relates to the corporate-wide advertising program is that the
16 rationale behind it as indicated in the last sentence of that
17 paragraph, is that the divisions with high revenues apparently
18 benefitted from the advertising more than the divisions with
19 lower revenues, and therefore ought to be allocated more --
20 more of the advertising costs; correct?

21 A. I think that's what Professor Horngren's book says, yes.

22 Q. Okay. And is that the same type of comparison that you
23 were doing in paragraph 48 as it related to the sales
24 compensation?

03:44 25 A. Well, I think the sales compensation passage -- and let

Holder - Cross - Stevens

03:44 1 me, if I may, get back to it; I set it aside. But I think
2 that was more in the realm of cause and effect than benefits
3 received, I think if I recall correctly. But having said that
4 I think there are elements that are intertwined in that
5 allocation basis of revenues, that are both related to cause
6 and effect, as well as benefits received. I did not identify
7 with specificity cost drivers.

03:44 8 Q. Okay. And as it relates to the reasonableness and
9 consistent basis of the allocated costs that was referenced in
10 footnote 2, it's your belief and understanding that you should
11 consider the result of the reasonableness of a cost related
12 allocation?

13 A. Yes, I think I testified generally to that to the extent
14 you're able to when I was providing my deposition.

03:45 15 Q. Okay. In fact, you should actually review the result for
16 reasonableness; correct?

17 A. Well, I think we ought to look at what I had to say. I
18 mean I think the ability to assess the reasonableness of any
19 complex process is a function of a great many variables, and
03:45 20 it ranges from being very specific in assessing
21 reasonableness, to only the most general considerations.

22 Q. And as it related to your review of the results of the
23 CAM, you didn't actually opine as to the reasonableness of the
24 costs that were assessed or allocated to the EQAT; correct?

03:45 25 A. I don't recall doing that. I think the focus of my

Holder - Cross - Stevens

1 opinion was on the reasonableness of the process that was
2 used, but again, in my deposition I think the person taking my
3 deposition raised questions about that, and I testified as I
4 indicated.

03:46

5 Q. Okay. So then it's a fair statement to say that you
6 didn't say the costs were reasonable, correct, that you were
7 focusing on the methodology?

8 A. I think that is generally a fair statement.

03:46

9 Q. And that's a statement that applies in this case;
10 correct?

11 A. I don't know what you mean by that.

12 Q. You said a generally fair statement; I just asked if you
13 said that you didn't say that the costs were reasonable.

03:46

14 A. I don't think I probably had a basis to make that
15 assertion. I did not audit the records of the company, PwC
16 audited them, I relied to some extent on the comfort provided
17 by their unqualified clean opinion that these were the costs
18 incurred. Yeah, that was way beyond the scope of anything I
19 was asked to do.

03:46

20 Q. And you're familiar with the external department slide
21 that's contained within P-210; correct? And I'll direct your
22 attention to page 4 of P-210. P-210 is the expense allocation
23 and methodology presentation.

03:47

24 A. I do have it in front of me now. What page did you
25 direct my attention to? I'm sorry.

Holder - Cross - Stevens

1 Q. Page 4.

2 A. Okay. I am -- I'm there.

3 Q. Okay. And as it relates to page 4 of this, did you ever
4 review this and assess in relationship to the Shared Services
5 Agreement?

6 A. I did, yes.

7 Q. Okay. And isn't it your testimony that you don't know
8 why this external department slide would not have been
9 contained within the Shared Services Agreement?

10 A. Well, no, I don't think that's quite a fair
11 characterization.

12 Q. Okay. I'd like to turn your attention to page 44 of your
13 deposition. If you look at -- it's actually 44 -- it begins
14 44-21; I'm just going to establish the foundation quickly to
15 show what you're looking at. It talks about Exhibit 6 --

16 THE COURT: So it's line 21?

17 MR. STEVENS: I'm sorry, your Honor, page 44, line
18 21.

19 THE COURT: Okay, thank you.

20 Q. The question is, okay, so we can go back -- I guess it's
21 page 34 in Exhibit 6 -- and they're talking about your expert
22 report, you understand that; correct? Because you were
23 talking about your expert report throughout the deposition;
24 right?

25 A. Well, I don't know throughout the deposition, but yes,

Holder - Cross - Stevens

1 I'll accept that you're referring to that there, or that the
2 questioner was referring to that.

3 Q. And then it actually continues and it says: 4, if you go
4 to page 45-8 -- so it's relating to page 4 of Exhibit 6 to
5 your deposition. Do you see that?

6 A. I do see that, yes.

7 Q. And you're discussing throughout the testimony the items
8 that are contained on the -- the services that are contained
9 on this exhibit; correct?

10 A. That's -- that's probably the case, I -- you know, let me
11 look. Page 4 of the exhibit, okay, yeah, it would appear to
12 be, yes.

13 Q. Okay, great. And you were asked the question on page 46,
14 line 6, it says: Assuming these costs aren't contained within
15 the \$14.4 million, which is your understanding, correct; you
16 said, that is my understanding.

17 Right?

18 A. Yes, that's -- that's correct.

19 Q. And your testimony has been that the \$14.4 million is a
20 direct and some indirect expenses that were assessed to FMG
21 pursuant to the Shared Services Agreement that exists between
22 FMG and AXA; correct?

23 A. I -- I think that's a fair characterization, yes.

24 Q. Okay. So then the answer to the question why wouldn't
25 they be included was: I don't know why they wouldn't include

Holder - Cross - Stevens

1 it.

2 Do you see that?

3 A. I see the words that you are -- that I said according to
4 this transcript, yes.

03:50 5 MR. HORA: Objection; there's more testimony in that
6 answer, that's not a complete answer.

7 THE COURT: Well, you'll have redirect.

8 BY MR. STEVENS:

9 Q. And so I'd like to now go back to page 15 of P-210, which
03:51 10 is the expense allocation -- the cost allocation methodology
11 that you were discussing -- we were discussing before.

12 A. I'm there.

13 Q. You're there; correct? Okay. On the left side there's a
14 box that says total AXA Equitable expenses; correct?

03:51 15 A. I see that. Yes.

16 Q. And did you review this report -- this specific
17 presentation as it related to how the specific numbers were
18 resulted or were gotten on the left column?

19 A. Generally, yes.

03:51 20 Q. So if I turn your attention to page 6 of that report,
21 it's entitled Expense Allocation 2012. Do you see that?

22 A. I see the page to which you're calling my attention.

23 Q. Okay. And up top it indicates that this is a
24 consolidating income statement management format; correct?

03:52 25 A. I see that, yes.

Holder - Cross - Stevens

1 Q. And it's your understanding that this was presented to
2 the Board; right?

3 A. I think it's part of this packet that was presented to
4 the Board.

03:52 5 Q. Okay.

6 A. That's my recollection.

7 Q. And I want to direct your attention to a line which is
8 about three-quarters of the way down the page entitled Total
9 Expenses.

03:52 10 A. I see that, yes.

11 Q. If you go all the way over to the right which is a total
12 column for 2012 --

13 A. Yes, sir.

14 Q. On that line for total expenses there's a number 1.615;
03:52 15 right?

16 A. I see that, yes.

17 Q. If you turn back to page 15, that reflects the 1.615
18 billion of total AXA Equitable expenses; correct?

19 A. That's my understanding, yes.

03:53 20 Q. Okay. And then on page 15 you have minus FMG direct
21 expenses 14.4 million; right?

22 A. That's what it says, yes.

23 Q. And that's pursuant to the Shared Services Agreement;
24 correct?

03:53 25 A. Those are charges that were assigned directly to the --

Holder - Cross - Stevens

1 through the Shared Services Agreement. They relate primarily
2 to those 50 or 51 employees, as I understand it.

3 Q. Right. And that was specifically to FMG; right? As a
4 business entity or for doing business with AXA; correct?

03:53 5 A. I don't take offense at your characterizations, yes.

6 Q. And are you aware as to whether or not AXA has any other
7 business entities that -- or associates that they expense or
8 will bill for work that they perform?

9 A. I'm not aware; I may have at one time been aware of that.

03:54 10 Q. Assuming they have some additional business entities
11 that they do expense, would you expect to see those expenses
12 also deducted from the total AXA Equitable expenses as it
13 relates to the expense allocation methodology?

14 (Brief pause.)

03:54 15 A. Could I hear that question again?

16 Q. The 14.4 million is a deduction based on a bill that they
17 gave to a business entity; correct, FMG?

18 A. Well, it's the expenses that were directly charged to
19 FMG, yes.

03:54 20 Q. Assuming there are other expenses directly charged to
21 other businesses by AXA, they would then also be reflected as
22 a minus from the total AXA Equitable expenses; correct?

23 A. Not necessarily -- not necessarily.

24 Q. Okay. These are the total AXA Equitable expenses;

03:55 25 correct?

Holder - Cross - Stevens

1 A. I have that general understanding.

2 Q. And if there were other expenses deducted from the total

3 AXA Equitable expenses, they should be reflected in this

4 slide, because if they're not that means that FMG is then

03:55 5 being allocated a portion of expenses that have already been

6 paid for by other businesses; correct?

7 THE COURT: Hold on a second; there's an objection.

8 MR. HORA: There's a foundation objection. I think

9 if he's got some sort of document that shows that, I think he

03:55 10 should show the witness rather than speculating.

11 THE COURT: You may answer the question if you

12 understood it, Doctor -- or Mr. Holder.

13 THE WITNESS: Unless there was some extenuating

14 circumstance, that would seem to follow.

03:55 15 BY MR. STEVENS:

16 Q. Okay, that's great. And then we have directly below that

17 the actuary DAC impact of 674.8; do you see that?

18 A. I do.

19 Q. And that actually gets added to the total AXA Equitable

03:55 20 expenses; correct?

21 A. Well, only -- I mean it's to remove its effects from the

22 AXA Equitable expenses, yes.

23 Q. Correct. And the effect by removing it is that it adds

24 AXA -- it adds expenses to the total AXA Equitable allocated

03:56 25 expenses that are then pushed down to my clients, the EQAT;

Holder - Cross - Stevens

1 correct?

2 A. No, I don't think that's correct.

3 Q. Well, the total AXA Equitable allocated expenses is 2.275

4 billion; correct?

03:56

5 A. I see that, yes.

6 Q. Okay. 1.615 billion minus 14.4, will come up with a

7 certain number; correct? Roughly 1.6 billion; right?

8 A. Okay.

9 Q. Is that correct?

03:56

10 A. 1.615.3 billion less 14.4 billion gives a little over a

11 billion 600 million.

12 Q. Right, okay. And then as it relates to that, if you add

13 in the 674.8 million, that would total up to the 2.275 billion

14 as reflected in the total AXA Equitable allocated expenses;

03:57

15 correct?

16 A. I think that generally follows.

17 Q. Okay.

18 A. But it's not appropriate to say that that removal of that

19 increases expenses. The expenses are what they are, and when

03:57

20 you --

21 Q. No; go ahead. Okay. Well, the removal of that as it

22 relates to the total AXA Equitable allocated expenses does

23 increase those expenses that are allocated; correct?

24 A. It increases the costs that are allocated by excluding

03:57

25 this DAC impact.

Holder - Cross - Stevens

1 Q. Okay. And are you aware as to how much of the -- I'm
2 sorry; you're aware that DAC means deferred acquisition costs;
3 correct?

4 A. I'm aware of that, yes.

03:57 5 Q. And are you aware of how much the -- how much deferred
6 acquisition costs were actually realized in the year 2012?

7 A. I -- I don't recall.

8 Q. Okay. Do you believe that it's the number that's
9 reflected there of roughly \$674 million?

03:58 10 A. I don't recall. I'd have to look back at some of the
11 underlying data.

12 Q. Let me ask you this. If it wasn't the \$674 million that
13 was realized, would that then call into question your
14 assessment of the cost allocation methodology?

03:58 15 A. No, I don't think so.

16 Q. So the fact that -- or not the fact, but the possibility
17 that \$674 million was included in the allocated expenses that
18 then were allocated down to my clients, does not impact your
19 view in any respect as it relates to the reliability of the
03:58 20 cost allocation methodology?

21 THE COURT: Wait a second.

22 MR. HORA: Objection; there's no foundation for the
23 statement that they're allocated down to his clients.

24 THE COURT: Do you understand the question, Mr.

03:58 25 Holder?

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1 THE WITNESS: At this point I'd need to hear it
2 again, your Honor.

3 THE COURT: So Frank, could you repeat question? So
4 I'll deny that motion.

03:59 5 (Question read back by the reporter.)

6 THE WITNESS: As I understand it, that wouldn't have
7 that effect. I mean there is an accounting process in which
8 deferred acquisition costs get amortized over a period of
9 time. There are actuarial evaluations of that also that take
10 place over time. The actuarial DAC impact here of -- that's
11 removed, is in my recollection at least, not part of the
12 normal amortization of DAC that exists, and that's
13 appropriate.

03:59 14 BY MR. STEVENS:

04:00 15 Q. So what I'm trying to -- you just said that that 674.8
16 million was not part of the actual amortization for the year
17 2012; correct?

18 A. Well, I guess I don't understand your question.

19 THE COURT: All right, then rephrase.

04:00 20 MR. STEVENS: That's fine, your Honor.

21 Q. I want to direction your attention quickly to page 6.

22 A. I am there.

23 Q. Of P-210?

24 A. Yes.

04:00 25 Q. And directly above the 1.615 there are certain numbers;

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1 do you see that?

2 A. I do.

3 Q. And it discusses -- the 1.65 is a total of all the

4 numbers that are contained directly above it, correct, in that

5 column?

6 A. Well, it's the net of those I think.

7 Q. Correct. And it's all those numbers all the way up to

8 the top beginning with the underlying investment margin?

9 A. Well, there's sub totals that are struck, so you can't

10 just add them all.

11 Q. So it's a total of the net revenues; correct?

12 A. No, it's not the total of the net revenues. It

13 incorporates the other things that are listed there as well.

14 Q. Understood. I was about to list them out, but it

15 incorporates what's in that column; correct?

16 A. I think that's a fair statement, yes, sir.

17 Q. Okay. And directly above the 1.615 there's two numbers;

18 right?

19 A. Yes.

20 Q. Amortization of DAC, deferred acquisition costs; correct?

21 A. Right.

22 Q. And that's 74 million; right?

23 A. I see that, yes.

24 Q. And amortization of VOBA, underlying results; do you see

25 that?

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1 A. The valuation of business acquired, yes.

2 Q. Right. And that's 4 million; correct?

3 A. I see that, yes.

4 Q. So that's a total of 78 million that's amortized for both
04:01 5 the DAC and VOBA for that year; correct?

6 A. That's my understanding.

7 Q. And then that additional money that's reflected of 674
8 million minus 78 million was not amortized for 2012; correct?

9 A. I don't understand that one, I'm sorry.

04:02 10 Q. Is it your understanding that based on the 74 and 4
11 million that 78 million of DAC and VOBA was amortized for
12 2012.

13 A. That's what that appears to reveal, the document which
14 you've drawn my attention.

04:02 15 Q. Okay. And as it relates the 674.8 million that was
16 reflected as DAC amortization on page 15 of P-210, that was
17 then put into the total AXA Equitable allocated expenses --
18 you see where I am; correct?

04:02 19 A. Yes, but that's -- the characterization of it on the
20 document is actuarial deferred acquisition costs impact, not
21 amortization.

22 Q. So then it's your position that they're merely putting
23 the impact of the additional 600 million of actuary DAC impact
24 in the allocated expenses; correct?

04:02 25 A. No, no, they're removing the effects from the expenses

Holder - Cross - Stevens

1 that were actually incurred.

2 Q. Right. And so in removing --

3 A. I'm sorry.

4 Q. In removing those that then adds, as we indicated, to the
5 total AXA Equitable expenses; correct?

6 A. No, the expenses are what they are, and this is -- this
7 number is contained in the two -- in the 1.615; and removing
8 its effects moves to the actual expenses incurred by AXA in
9 providing these services to the 2.275 billion as I understand
10 it.

11 Q. So then is it your understanding of the cost allocation
12 methodology that the amount of expenses that are then put
13 through step A, B and C is not 2.275 billion?

14 A. No, I didn't say that.

15 Q. Okay. So then we're talking on -- we're together that
16 2.275 billion is the total AXA Equitable expenses that are
17 then allocated down eventually to the EQAT.

18 A. I think that's a fair statement.

19 Q. Okay. So if I can direct your attention to Defense
20 Exhibit 1510. And that's the EITF 99-19.

21 THE COURT: Mr. Holder, here you go.

22 THE WITNESS: Thank you.

23 I have it.

24 Q. Okay. And this is part of what you used to suggest that
25 the sub-advisory and sub-administrative fees were

Holder - Cross - Stevens

1 appropriately assessed as expenses; correct?

2 A. Appropriately reflected as --

3 Q. Reflected as expenses; correct?

4 A. Yes, this is part of the collection of information I used
5 in arriving at that judgment, yes.

6 Q. Okay. And if we look at the first page of that document,
7 this is a document that is actually by the Financial
8 Accounting Standards Board; correct?

9 A. Yes, I think that's a fair statement. The EITF is a
10 committee or a group established by and that reports to the
11 Financial Accounting Standards Board.

12 Q. Okay. And then as it relates to the financial -- the
13 financial accounting, you've already indicated that there's a
14 difference between management accounting and financial
15 accounting; correct?

16 A. There are differences, sure.

17 Q. And are you aware that this specific EITF 99-19 was
18 superseded in 2014?

19 A. No, it really wasn't. I mean I can't accept your
20 characterization of what transpired.

21 Q. And why is that?

22 A. Well, because there's a -- the FASB had been working for
23 year and years and years on a major revenue recognition
24 project, and they issued a new standard on revenue recognition
25 that was very broad and very pervasive in its effect. That

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1 standard has not yet become effective, and will become
2 effective for SEC registrants only -- well, it will be
3 effective in the next year; it will be effective for other
4 entities in the years following that.

04:06

5 I did look at the -- as part of my preparation here, at
6 the portion of that new standard that helps distinguish
7 between those costs that should be treated as a reduction of
8 revenue versus those that should be treated as an expense, and
9 I performed that analysis and came to the same conclusion

04:06

10 there are fewer indicators of --

11 MR. STEVENS: If I could just object, your Honor --

12 THE COURT: Well, wait; let him finish the answer.

13 MR. STEVENS: The only concern I have, Judge, is I
14 have about two minutes left so I wanted to quickly get in --

04:07

15 THE COURT: You asked the question, so we might as
16 well get the answer.

17 MR. STEVENS: I didn't expect it to be so long.

18 THE COURT: So Mr. Holder, you may continue.

19 THE WITNESS: That supersession, which is not yet

04:07

20 effective, restated the indicators of reporting net versus
21 reporting gross, in my view it did not change them
22 substantively. And in the instant case I still think that the
23 revenue, even if this new standard was effective today or --
24 and it's not, or back in 2012 and it's not, you would still

04:07

25 get the same result, that these costs should be reported as an

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1 expense and not as a reduction of revenue.

2 BY MR. STEVENS:

3 Q. Okay. And that's for financial reporting; correct?

4 A. Well, it's for -- well, all of it is financial reporting.

04:07 5 I mean managerial accounting relies on financial reports.

6 Q. And your opinion based on this is that this specific

7 standard applies the FMG; correct?

8 A. I think FMG would use this standard and its predecessor

9 which was identical, and when the new one becomes effective

04:08 10 they will use it, in their financial reports which are

11 presented in conformity with GAAP.

12 Q. Okay. I want to direct your attention to page 3 of this

13 document.

14 A. I am there.

04:08 15 Q. And that is -- the top part is where you indicated that

16 -- I believe that you believe that FMG fell within the

17 confines of this -- of this EITF; correct?

18 A. Well, I think you need to read the whole EITF in its

19 entirety and understand it collectively. The part I alluded

04:08 20 to, though, begins on page 4 where the title indicators are

21 gross revenue reporting, and the next eight paragraphs march

22 through each of those, the first one there paragraph 7 is the

23 company's the primary obligor, the second one's the inventory

24 thing, but that's what I referred to, not page 3 specifically.

04:09 25 But I think you ought to read the entire document as you try

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1 to understand it and implement it.

2 Q. Okay. And that was within -- you did that in what is
3 your the demonstrative exhibit Defendant's Exhibit 2053 which
4 references FASB 605-45; correct?

04:09 5 A. Yes, sir.

6 Q. And as it relates then to FMG, if FMG wasn't excluded
7 from this regulation, then it would be inappropriate to report
8 the sub-advisory fee and sub-administration fee as expenses
9 pursuant to this; correct?

04:09 10 A. If this didn't -- I'm sorry.

11 MR. HORA: I was just going to say objection, lack
12 of foundation.

13 THE COURT: Frank, can you repeat the question?
14 (Question read back by the reporter.)

04:09 15 THE COURT: Can you explain what you --

16 MR. HORA: I just don't know what basis he has to
17 suggest that FMG's excluded from this guidance.

18 MR. STEVENS: I'll get there, Judge.

19 THE COURT: So you're going to go through this
04:10 20 issue?

21 MR. STEVENS: I am.

22 THE COURT: Okay. You may.

23 BY MR. STEVENS:

24 Q. Okay. So as it relates -- I want you to look at
04:10 25 paragraph 4 on page 3.

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1 A. I'm sorry; page 4 of?

2 Q. Paragraph 4 on page 3 of the EITF 99-9 (sic).

3 A. Yes, yes.

4 Q. And paragraph 4 says: This issue -- and that's relating
5 to the EITF; correct?

6 A. Yes.

7 Q. Excludes from a scope transactions for which guidance is
8 provided by categories A and B above of the GAAP hierarchy.
9 Correct?

10 A. You've read that accurately, yes.

11 Q. Including -- and I want you to skip down to the fourth
12 bullet point. Do you see that?

13 A. I do, yes.

14 Q. And it says: Revenue transactions in specialized
15 industries addressed in AICPA accounting and auditing guides,
16 and in then parentheses, for example, airlines, casinos,
17 investment companies and so on. Do you see that?

18 A. I do.

19 Q. So if FMG pursuant to the FASB is treated as an
20 investment company, then they would be excluded from the
21 guidelines of the EITF; correct?

22 MR. HORA: Objection; foundation. FMG is not an
23 investment company. There is no foundation for him to suggest
24 that it's an investment company. That's...

25 THE COURT: Have you finished your argument?

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1 MR. HORA: I have, yes.

2 THE COURT: All right. Mr. Stevens?

3 MR. STEVENS: There's going -- I'm going to direct

4 him to the specific provision that's going to say that

04:11 5 pursuant to FASB, which is what I referenced, which is what

6 these EITFs are generated from and guidance from, would define

7 FMG as an investment company pursuant to the FASB.

8 THE COURT: So, I don't recall this ever coming up

9 during the course of the trial to tell you the truth.

04:12 10 But, Mr. Holder, do you believe that -- or do you

11 have an opinion as to whether or not FMG is an investment

12 company, under these guidelines?

13 THE WITNESS: Well, it doesn't say this here. I

14 mean investment companies typically get characterized as those

04:12 15 covered by the Investment Company Act of 1940. What I can

16 tell you I did do in answer to your question, and I think it

17 is pertinent, is I did look at the investment company's

18 accounting and audit guide, and I did look at the insurance

19 company's accounting and audit guide, although I don't believe

04:13 20 it is mentioned here, although insurance and reinsurance

21 premiums are, and I did not find guidance for this kind of a

22 transaction in those guides.

23 MR. STEVENS: So if I could then, your Honor, direct

24 his attention to what I've had premarked as P-787.

04:13 25 THE COURT: Does your adversaries have a copy of

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1 this?

2 MR. STEVENS: They do, your Honor.

3 BY MR. STEVENS:

04:13 4 Q. And Dr. Holder, are you familiar with this document in
5 any way?

6 A. Generally, yes.

7 Q. And it's actually a FASB accounting standards update;
8 correct?

9 A. It is, yes.

04:13 10 Q. And it's entitled Financial Services Investment
11 Companies; correct?

12 A. I see that, yes.

13 Q. Okay. I want to turn your attention to page 12, of this
14 document.

04:13 15 A. I am there.

16 Q. Page 12 begins, assessment of investment company status.
17 Correct?

18 A. I see that, yes.

04:14 19 Q. And it defines pursuant to number 946-10-15-4, that: An
20 entity regulated under the Investment Company Act of 1940 is
21 an investment company under this topic. Do you see that?

22 A. Yes.

23 Q. And that's the FASB guidance as it relates to investment
24 company status; correct?

04:14 25 A. Yes.

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1 Q. Okay, thank you. As it relates to that document I just
2 showed you, is this a document that -- the FASB accounting
3 standards update, is this a document that's relied on by
4 individuals in your field?

04:14 5 A. Yes, working in the appropriate realm, yes.

6 Q. Okay. Is it authoritative as it relates to the
7 accounting standards pursuant to the FASB?

8 A. It's an authoritative part of generally accepted
9 accounting principles, yes.

04:15 10 Q. And as you indicated you're familiar with this --

11 MR. STEVENS: Your Honor, at this time plaintiffs
12 would move into evidence P-787.

13 THE COURT: P-787?

14 MR. STEVENS: Yes, your Honor.

04:15 15 THE COURT: Any objections?

16 MR. HORA: No objection.

17 THE COURT: All right, admitted.

18 (Plaintiff's Exhibit 787 was marked into evidence.)

19 BY MR. STEVENS:

04:15 20 Q. And you're aware that FMG uses the result of its cost
21 allocation methodology, which we've just been talking about,
22 in their profitability analysis that's presented to the EQAT
23 Board; correct?

24 A. I understand that, yes.

04:15 25 Q. And are you also aware that they do not report the

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1 roughly 49 million of allocated expenses that result from the
2 FMG-CAM on their audited financial statements?

3 A. I have that understanding.

4 Q. Okay. And are you also aware then that FMG never

04:16 5 actually pays a \$49 million in allocated expenses to AXA?

6 A. I don't recall seeing documents or evidence that suggests
7 that they do.

8 Q. So then basically the only reason for the cost allocation
9 methodology is to report profitability to the Board; correct?

04:16 10 A. I don't know if that's the only reason, but it's one that
11 I understand exists.

12 Q. Okay. And by including the \$49 million as expenses in
13 its presentation to the Board, that decreases the profit FMG

14 reports to the Board related to the services rendered to the
04:16 15 EQAT under the Investment Management Agreement as well as the
16 Administration Agreement; correct?

17 A. Yes. The profitability analyses, or at least some of
18 them I looked at, don't show the portions of those 49 million
19 for individual elements of that, but eventually down at the

04:17 20 bottom they are included in the overall profitability
21 assessment.

22 Q. And also including those costs then of 49 million would
23 also decrease the profit margin FMG reports to the Board;
24 correct?

04:17 25 A. That would have that effect, yes.

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1 MR. STEVENS: I have nothing further, your Honor.

2 THE COURT: All right. Redirect?

3 MR. HORA: I don't have any questions.

4 THE COURT: Okay. So, wait; don't step down yet,

04:17 5 Mr. Holder. You testified a bit about the DAC.

6 THE WITNESS: Yes, sir.

7 THE COURT: All right. Could you just go through

8 how that DAC and the formula that's used for cost allocation

9 works? You know I'm a novice at this; I've been spending six

04:17 10 weeks here, but we've heard a lot about DAC and they testified

11 about it. But if you could, just tell me how it works in this

12 cost allocation issue.

13 THE WITNESS: Sure. Deferred acquisition costs, or

14 DAC, arise when there's an origination of insurance policies,

04:18 15 other investment vehicles. Compensation may be paid, for

16 example, to an agent that placed the policy up front; and yet

17 that compensation is going to benefit the paying company, say

18 AXA, over a relatively long period of time.

19 THE COURT: I see.

04:18 20 THE WITNESS: There are a number of actuarial

21 assumptions that go into the period over which, as I

22 understand it at least, DAC gets allocated generally. And in

23 the questions that were being posed to me, there were a couple

24 of those that are the normal DAC allocation, that is done to

04:18 25 amortize those -- those deferred acquisition costs that will

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1 appear on a balance sheet, over a period of time.

2 THE COURT: A period of years.

3 THE WITNESS: There is a management function that

4 frequently requires actuarial evaluation, and it doesn't

04:19 5 necessarily require entry into the -- to the accounting

6 records, but there's also a number of calculations that will

7 update the actuarial assumption from time to time. As I

8 understand it, and there are better people to explain this

9 down at this level than me I think from the company, but

04:19 10 essentially, those actuarial adjustments are not considered

11 part of the day-to-day business of AXA; they're not the kinds

12 of transactions like paying someone a salary to render

13 services, whether that's one of these 50 people or whether

14 it's someone in data processing or in shareholder -- you know,

04:20 15 the amortization of DAC that is calculated does become part of

16 that expense stream.

17 The actuarial valuations that occur is this large

18 674 million that is excluded = from the recurring operating

19 expenses, the business based expenses of AXA, as I understand

04:20 20 it, your Honor.

21 THE COURT: All right. So when you're doing this

22 cost allocation, how does this impact how it affects the

23 Board? Is that too --

24 THE WITNESS: No, sir, I certainly --

04:20 25 THE COURT: Do you understand what I'm trying to get

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1 to?

2 THE WITNESS: No, your Honor --

3 THE COURT: I was trying to figure out if the Board
4 members are sitting there, and they're confronted with this
04:20 5 cost allocation theory, and they're looking at this DAC, what
6 impact does the DAC have on the cost allocations? And I guess
7 what happens with the -- they're watchdogs for investors; so
8 what happens to the investor?

9 THE WITNESS: I would hesitate to -- and I would not
04:21 10 try to speak as to what goes on in their minds and so on. I
11 can speak to the information that's presented to them, and
12 certainly Board members, you know, have an obligation to probe
13 and raise questions in my own view at least, when they're
14 hearing information, when they're receiving information,
04:21 15 having said all of that the information shows that DAC
16 adjustment, it shows it being removed from the daily operating
17 expenses; that DAC adjustment could go the other way. It
18 could reduce expenses, as well as increase expenses through
19 its presence.

04:22 20 And so when you remove its effects that could
21 cause the -- well, it wouldn't cause it without taking great
22 exception to that, but the costs that remain to be allocated
23 could be greater or less than the costs to be allocated with
24 that DAC actuarial adjustment in it. But the primary reason
04:22 25 it's excluded is it's a valuation, not part of the

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1 amortization of the costs that in fact were paid, and that are
2 being charged over a period of time.

3 THE COURT: All right. So they're deleting the DAC
4 from the cost allocation that -- of the expenses that are
04:22 5 borne by the investors?

6 THE WITNESS: They are -- they are eliminating this
7 actuarial DAC adjustment, but not the DAC amortization.

8 THE COURT: The adjustment. So that's the one that
9 doesn't happen in the ordinary course of day-to-day --

04:23 10 THE WITNESS: That is my understanding yes, your
11 Honor.

12 THE COURT: Okay, thank you. So, you know, we're
13 here looking at this -- the plaintiffs have this suit, that
14 the Board of the funds has breached a fiduciary duty to their
04:23 15 investors because they've allowed these expenses. And I'm
16 oversimplifying this, but they've allowed these expenses of
17 FMG that are beyond reasonable.

18 So, from looking at the documents in this case, do
19 you think that the Board has been presented with the
04:23 20 appropriate types of documents necessary to evaluate those
21 expenses?

22 THE WITNESS: Obviously this Board, like any board,
23 is dependent upon the information that flows from management.
24 They will take comfort from the audit opinion expressed by the
04:24 25 internal -- by the external independent auditor on its

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1 financial statements; they will take comfort from reports they
2 received from internal audit.

3 This process of allocation that has occurred I
4 think, it seems to me it was explained to the Board members in
04:24 5 a way that was lucid and sufficiently informative to allow a
6 Board member to raise questions if they didn't understand some
7 of the things being presented in these documents that weren't
8 clear to them.

9 THE COURT: So, the entire case comes -- well, I
04:24 10 shouldn't say the entire case. But what always happens is we
11 get back down to the basis points and the fees that are
12 charged. So, we're always trying to get back to well, are the
13 basis points for the fee charged within this reasonableness
14 factor as to what other funds, not controlled by FMG, are
04:25 15 doing and things -- what the other people in the industry are
16 doing. And do you think the information the Board had shows
17 that type of differentiation well enough? If you know.

18 THE WITNESS: I don't know what information might
19 have gone to the Board about other companies in the industry,
04:25 20 and, you know, the competitive pressures under which AXA might
21 be operating to price its products in a way that, you know,
22 would be attractive to investors. So I'm -- I'm unaware of
23 that.

24 I do think that the Board would have become aware of
04:26 25 the total costs incurred by AXA, and that would have been

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04:26 1 considered reasonable -- reasonably considered. It would have
2 been reasonable to consider those costs reliable; I think
3 there is the disclosure of the DAC exclusion; I -- I think the
4 cost allocation process based on these documents was explained
5 in sufficient detail, that someone could comprehend what was
6 going on.

7 THE COURT: All right.

8 THE WITNESS: I hesitate to go further.

04:26 9 THE COURT: No, that's fine. I had one more
10 question. So, from your review of the industry -- and I
11 suppose what we're talking about AXA type of companies, and
12 these variable annuities that they have and things of that
13 nature; so, do you think that competitors of FMG or AXA let's
14 say, that they would have the same type of profitability
04:27 15 calculations that were being used in this case? You know,
16 like the DAC, for instance, do you think they all have this
17 DAC issue?

04:27 18 THE WITNESS: They probably all have the DAC issue,
19 because that's just part of the process, it's part of the
20 actuarial work that is necessary, all the way down to pricing
21 products. How they treat it, how they assess profitability,
22 your Honor, I -- I don't have that general knowledge. I feel
23 obviously rather strongly about if these costs are
24 appropriately allocated, the manner in which they're presented
04:28 25 as an expense rather than a reduction of revenue, makes --

James - Direct - Hood

1 makes sense. It's entirely appropriate.

2 THE COURT: All right, thank you. You may step
3 down.

4 (Witness excused.)

04:28 5 THE COURT: Next witness?

6 MR. MURPHY: Your Honor, I believe Ms. Hood will
7 introduce herself. I believe we're going to call our next
8 expert, Mr. Chris James to the stand.

9 (CHRISTOPHER M. JAMES, Ph.D.), affirmed.

04:29 10 THE COURT: Could you just spell your last name once
11 you're seated?

12 THE WITNESS: My Last name is spelled J-a-m-e-s,
13 first name Christopher.

14 THE COURT: Thank you.

04:30 15 MS. HOOD: Your Honor, before I begin, since this is
16 my first appearance in this trial, I'd just like to introduce
17 myself; I'm Andrea Hood with the Milbank firm on behalf
18 defendants.

19 THE COURT: Good afternoon, Ms. Hood.

04:30 20 MS. HOOD: Thank you. May I?

21 THE COURT: You may. Please start.

22 MS. HOOD: Thank you.

23 (DIRECT EXAMINATION OF CHRISTOPHER M. JAMES, Ph.D. BY MS.
24 HOOD:)

04:30 25 Q. Dr. James, what is your current occupation?

James - Direct - Hood

1 A. I'm a professor of finance, I have two appointments
2 currently, one at Cambridge University in the UK, and the
3 other at the University of Florida, where I'm the William H.
4 Dial Eminent Scholar in Finance.

04:30 5 Q. And how long have you held your position at the
6 University of Florida?

7 A. My daughter's 26; so 26 years.

8 Q. And how about at the University of Cambridge?

9 A. I've been there since the fall, last fall.

04:31 10 Q. Dr. James, can you please tell the Court about your
11 educational background beginning with college?

12 A. Sure. I have an undergraduate degree in economics and
13 mathematics, Master's in business administration and finance,
14 and a PhD in economics, specializing in industrial
04:31 15 organization, finance, and applied statistical analysis.

16 Q. And from what academic institution did you receive your
17 BA?

18 A. From Michigan State University.

19 Q. And your MBA?

04:31 20 A. From the University of Michigan.

21 Q. And your PhD?

22 A. Another Michigan institution, University of Michigan.

23 Q. And when did you receive your PhD in economics?

24 A. I received my PhD in 1978.

04:31 25 Q. Since receiving your PhD in 1978, have all of your

James - Direct - Hood

1 employment positions been in the area of economics?

2 A. Finance and economics, yes. Primarily in the area of
3 finance as it applies to financial institutions such as banks,
4 mutual funds, insurance companies, that type of thing.

04:32 5 Q. And have you ever been involved in government service?

6 A. I have, I've had several stints with the government, I
7 can do it in reverse chronological order if you'd like. From
8 2008 to 2014 I was a scholar at the San Francisco Federal
9 Reserve Bank, advising the President on issues regarding
04:32 10 primarily capital management at banks, under the regulatory
11 purview of the San Francisco Fed, as well as some issues
12 arising from the financial crisis.

13 Prior to that I held appointments at the Federal
14 Reserve Bank Board of Governors.

04:33 15 MR. MURPHY: I'm just go to move your mic a little.

16 A. Okay. I have held several appointments at the Federal
17 Reserve Bank -- Federal Reserve Board of Governors as a
18 consultant on issues regarding regulatory policy. Prior to
19 that at the FDIC, Federal Deposit Insurance Corporation,
04:33 20 again, as a consultant; and then at the U.S. Department of
21 Treasury as a senior economic advisor to the Comptroller of
22 the Currency, advising the comptroller on economic matters
23 that arose in the regulation and examination and oversight of
24 commercial banks and financial institutions.

04:33 25 I've also held what I'll call a quasi government

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04:34 1 position; I was appointed and approved by the SEC as an
2 independent distribution consultant for the Janus Funds to
3 administer a fair fund settlement over a period of about four
4 years. Janus Funds are mutual funds that were subject to a
5 regulatory settlement, and my job was to determine the
6 appropriateness of various allocation schemes, and to if
7 disagreements arose between the Janus Funds and the SEC as to
8 the appropriateness of a particular allocation, that I was the
9 arbitrator.

04:34 10 In addition I've worked as a consultant for -- at the
11 Office of the Chief Economist at the SEC, on issues regarding
12 mutual fund pricing and performance issues.

04:35 13 Q. Okay, thank you. And I just want to break that down a
14 little bit and see if we can provide the Court with a little
15 more detail regarding what your responsibilities were in each
16 of those government service capacities.

17 A. Sure.

04:35 18 Q. So, with respect to your -- before I get to that, all of
19 these positions that you've just described that you've held in
20 government service capacity, they've all been in the capacity
21 of a financial economist?

22 A. Yes.

04:35 23 Q. You mentioned that you've held a role with the Department
24 of Treasury; can you provide any detail as to -- any
25 additional detail as to what your responsibilities were there?

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04:36 1 A. Sure. The Comptroller of the Currency is the primary
2 regulator of national banks, and as a senior advisor to the
3 comptroller I would advise -- it was John Heimann at the time;
4 on issues regarding either regulatory developments or
5 proposals, examination practices as it pertains to banks. So,
6 for example, when I was at the comptroller's office, one of
7 the issues was the extent to which it might be appropriate to
8 have commercial banks through their holding company serve as
9 asset management firms, broadening the bank product offerings.

04:36 10 And so we looked very carefully at, for example, what
11 implications those types of activities would have for the
12 safety and soundness of the banks that we regulated, what
13 issues arose with respect to the risks that the bank would be
14 subject to; if they engaged in asset management, and as well
04:37 15 as potential synergies with other services or activities that
16 the bank engaged in.

17 Q. And I believe I just heard you refer to asset management
18 firms; when you referred to asset management firms is that
19 term synonymous with an investment manager like FMG?

04:37 20 A. Yes. So, the issue is really should banks be able to
21 provide mutual fund products to their customers, and serve as
22 an investment manager and administrator for those products.

23 Q. And you just went through some of your responsibilities
24 in your role as a scholar and consultant at the Federal
04:37 25 Reserve Bank in San Francisco?

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1 A. Right.

2 Q. With respect to that role, can you provide anymore detail
3 about your responsibilities there that perhaps would be
4 relevant in this case?

04:38

5 A. Sure. The banks and holding companies are regulated in
6 part based on the amount of capital that they have. The idea
7 is to have capital sufficient to cover potential losses
8 arising from say operational issues or increased losses and
9 the like. And I've been part of a team that has evaluated the
10 adequacy of both the risk management systems, as well as the
11 capital of major banks within the regulatory purview of the
12 San Francisco Federal Reserve.

04:38

13 And that would include looking at risk management
14 issues as it pertains both to the bank itself, as well as in a
15 holding company context subsidiaries that, for example, a bank
16 like Wells Fargo offers mutual funds, and serves as an
17 investment manager for some of its funds, and then sub-advises
18 out of those funds.

04:38

19 Q. And in that capacity in looking at the risks that an
20 investment manager that's housed within a bank might face,
21 what types of risks do you look at?

04:39

22 A. We typically look at -- it goes by various terms,
23 sometimes it's referred to as operational risk, sometimes it's
24 referred to as business risk, under the risk-based capital
25 standards that are applied to banks we call it operational

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1 risk; so those are things such as risks arising from
2 operational failures or mistakes. Certainly reputational
3 risks that arise from either those operational mistakes or
4 poor product performance.

04:39

5 In addition, regulatory and litigation related risks
6 that may impose losses on the bank. As well as, you know,
7 risk in terms of the operation of the businesses to the extent
8 that you say you have a large decline in the volume of
9 business, what implication would that have in terms of the

04:40

10 company's ability to earn a profit.

11 Q. And can you describe for the Court how it came about that
12 you came became involved in analyzing these types of risks
13 while you were at the Federal Reserve?

04:40

14 A. Sure. That's part and parcel of what I do as a financial
15 economist and what I teach my students when I teach financial
16 institutions management courses. With respect to operational
17 risks, I was a part of a major project that was undertaken at
18 the Bank of America to assess operational risks in primarily
19 it's non-bank activities, so it's in trust activities, for
20 example, and other non-bank related activities.

04:41

21 I wrote a paper that's been widely cited on how you go
22 about measuring operational risks, and how they should be
23 considered in terms of evaluating say the profitability of a
24 financial institution. And it was through that work that, you
25 know, I did a number of presentations, some at the Federal

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1 Reserve, and one thing led to another and I've been doing it
2 ever since.

3 Q. You also mentioned that you've in I believe two stints
4 have held consulting positions with the Office of the Chief
04:41 5 Economist at the SEC?

6 A. Yes, I was brought in on a couple of occasions to address
7 certain issues that the chief economist, who's the -- as the
8 name suggests, the chief advisor to the commission on economic
9 management. One had to do with issues called soft dollar
04:42 10 brokerage, the payment for research services, by mutual funds
11 and their advisors.

12 The second was to do with issues concerning pricing of
13 mutual fund underlying portfolios, to ensure that the net
14 asset value, which is what's posted at the end of each day
04:42 15 where you buy and sell a mutual fund at, is not stale, meaning
16 it reflects accurately the value of the underlying portfolio
17 of a mutual fund.

18 Q. And you also mentioned that you served as the independent
19 distribution consultant for the Janus Funds; what was the time
04:43 20 period where you've held that position?

21 A. 2003 to 2006 I believe.

22 Q. And can you provide a little more detail on what your
23 responsibilities were as the independent distribution
24 consultant for the Janus Funds?

04:43 25 A. Yes. I was approved by the SEC to manage what's called a

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04:43 1 fair fund settlement, which was a hundred million dollar
 2 settlement that Janus entered into with the SEC pertaining to
 3 damages that arose from allowing what are called market timers
 4 to come into the fund and trade in and out of the various
 5 mutual funds. And both to assess the damage that was caused
 6 by that, to allocate it to fund holders, in a way that was
 7 reasonably related to the harm that was caused by having this
 8 rapid trading in and out of mutual funds by certain large
 9 investors.

04:44 10 Q. And moving away from your roles in government service,
 11 and without revealing any confidential information, have you
 12 done any -- have you ever been hired by investment managers to
 13 perform any consulting work?

04:44 14 A. I have, I've been hired by several complexes to address
 15 issues concerning certainly pricing issues, meaning fee
 16 related issues; and risk assessment issues, in other words,
 17 assessing risk exposure at various of the complexes; as well
 18 as working on some product development issues.

04:45 19 Q. Did any of your consulting work involve in any way
 20 economies of scale?

 21 A. Oh, sure. When -- when looking at and examining some of
 22 the fee structures at the various complexes that I've been
 23 employed at to look at issues regarding, for example,
 24 profitability, the cost structure, how cost structures might
04:45 25 change as the scale of operation changes.

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1 Q. And prior to your current academic positions at the
2 University of Florida and the University of Cambridge, have
3 you held academic positions at any other universities?

04:45 4 A. I have, I've taught at -- in terms of full-time at other
5 institutions, such as the University of New South Wales, the
6 University of Oregon, and the University of Michigan.

7 Q. And have all those positions been as a professor of
8 economics or finance?

9 A. They have been.

04:46 10 Q. And you've taught courses in those positions?

11 A. I've taught courses, my coursework focuses primarily on a
12 couple of issues; generally corporate finance, so

13 corporation's finance and sales. I tell a teach a course in
14 financial institutions, which is the economics and management
04:46 15 of financial institutions, such as banks, mutual funds,

16 insurance companies, hedge funds, private equity funds; and I
17 teach a course in what's called organizations in markets,
18 which is a course that is really targeted towards Master's and
19 business administration students on industrial organization;

04:46 20 what factors determine an organization size, the extent to
21 which it out-sources versus in-source, that type of thing.

22 Q. And the courses you've taught, at what levels have they
23 been at?

04:47 24 A. For the last 24 years it's been graduate students, either
25 Master's or PhD level. I've taught early in my career

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1 undergraduates, but I haven't done that in a while.

2 Q. And have you authored any articles as an economist?

3 A. Yes, I am actively engaged in research; I think I've

4 published in my career in terms of peer-reviewed scholarly

04:47 5 journals maybe over 50, and in other publications another 50.

6 Q. And without going through every publication, can you give

7 the Court a sense of what subject matters your publications

8 have addressed?

9 A. They focused primarily again on financial institutions;

04:48 10 some issues -- papers on that address issues in banking;

11 papers that address issues in terms of risk management; papers

12 that address issues in terms of mutual fund performance

13 evaluation, and structure; so it's across a wide range of

14 areas.

04:48 15 Q. Dr. James, do you hold any -- do you serve on any

16 editorial boards?

17 A. I do. I currently serve I believe on five boards, and

18 have served on pretty much have every -- each one of the top

19 tiered journals in my field, as either an associate editor, or

04:48 20 as the editor.

21 Q. And what are some of those journals?

22 A. The Journal of Finance; the Journal of Financial

23 Economics; the Journal of Financial and Quantitative Analysis;

24 the Journal of Financial Services Research; the Journal of

04:49 25 Financial Mediation, which is a journal targeted towards

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1 issues regarding financial institutions; the Journal of
2 Economics and Decision Science; there's a couple others, but
3 that's what comes to mind as I sit here.

04:49 4 Q. And what are your responsibilities on these editorial
5 boards?

6 A. The editorial board serves as a -- really a gatekeeper,
7 with the editor or associate editor typically makes a decision
8 as to who will review a paper, and then ultimately the
9 decision as to whether the publish a paper is made by the
10 editor or one of the associate editors. And that decision is
11 based on, you know, whether the study advances our knowledge
12 in a particular area in a significant way, and whether the
13 paper employs methodologies that are consistent with the
14 scientific method in my field.

04:50 15 Q. And have any of the proposed articles you've had to deal
16 with as an editor or associate editor on these boards dealt
17 with mutual funds?

04:50 18 A. A number of them have. Having a specialization in
19 financial institutions, when I'm on the board I get most of
20 the papers that deal with financial institutions. So, when I
21 was associate editor at the Journal of Finance, I'd get maybe
22 25 manuscripts on issues regarding mutual funds in a one or
23 two year time period. Similarly, with the Journal of
24 Financial Economics, most of the papers that I either referee
04:51 25 myself or advise on publication are papers in the financial

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1 institutions area.

2 Q. Dr. James, have you ever been permitted to testify as an
3 expert witness at trial?

4 A. I have.

04:51 5 Q. And approximately how many times?

6 A. I've been -- I've been in the profession a long time;
7 about 25 times.

8 Q. And by what tribunals have you been permitted to testify?

04:51 9 A. Certainly in federal courts, state court, SEC
10 proceedings; that's what comes to mind.

11 Q. And has that all been as an economist?

12 A. Yes.

13 Q. So recognizing that we've probably gone through some of
14 this already in going through your prior experience and
04:52 15 positions that you've held, can you describe for the Court
16 what, if any, experience you have relating to economies of
17 scale?

18 A. Oh, well, my -- that begins back when I was a PhD student
19 at the University of Michigan, my field was industrial
04:52 20 organization; one of the first papers I did in order to
21 advance to candidacy was on economies of scale, measurement,
22 both in terms of analysis statistical analysis of the
23 relationship between scale of operation and costs, as well as
24 applying what was called a survivor technique to look at,
04:52 25 where whether within a particular industry's firm's clustered

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04:53 1 at a particular size, that would suggest that that's the size
2 in which most economies of scale are realized; or the size
3 distribution of firms distributed along a wide range
4 suggesting that there's really no significant economies of
5 scale, because you have small firms in the industry and big
6 firms in the industry and they compete with one another and
7 survive.

8 Q. And are there any other -- is there any experience you've
9 had that's related to economies of scale?

04:53 10 A. I certainly looked at those issues as I mentioned in a
11 consulting context, and those were issues, you know, that we
12 looked at quite carefully when I was at the comptroller's
13 office and in other work I've a done at the government
14 agencies.

04:53 15 Q. And somewhat relatedly, what if any experience do you
16 have relating to the extent to which economies of scale can --
17 in the investment management context, can be shared with fund
18 investors through breakpoints in the fund's fee schedules?

04:54 19 A. That's something I've certainly looked at in this case,
20 and I've looked at both in other cases as well as in a
21 consulting role.

22 Q. And again, without revealing any confidential
23 information, can you generally describe how that analysis of
24 breakpoints as they relate to economies of scale would work?

04:54 25 A. Sure. The economies of scale, so we're clear, refer to

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04:55 1 how total unit costs change as the volume of a particular
2 product increases; so as scale of operation increases, what
3 happens to total unit costs. And we say that there are
4 economies of scale if you observe declines in total unit cost
5 as a scale of operation increases.

6 And often times you'll find situations in which either
7 there are economies of scale in a particular range of
8 operation, or scale of operation, and then diseconomies of
9 scale, meaning unit costs are actually increasing as the scale
04:55 10 of operation increases.

11 So, it's really about looking at, to the extent that's
12 possible, of looking at unit costs. You get some insights
13 into the existence of economies of scale by looking at the
14 structure of an industry, so if you see lots of firms within
04:55 15 an industry with varying size ranges, and you see a
16 distribution of fees across a variety of size ranges, that's
17 going to give you some indirect evidence of whether or not
18 economies of scale exists.

19 Q. And as a general matter, again, without revealing any
04:56 20 confidential information from your prior consulting jobs,
21 how -- how in the past have you analyzed how breakpoints fit
22 into what you just described, breakpoints in the fund's fee
23 schedules?

24 MR. A. LAKIND: Your Honor, I'm sorry to interrupt;
04:56 25 is this beyond the voir dire? I'm not sure if this is beyond

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1 the voir dire or we kind of morphed into direct --

2 THE COURT: Ms. Hood hasn't offered the doctor as an
3 expert witness yet, so I thought we're still doing the voir
4 dire.

04:56

5 Is that right, Ms. Hood?

6 MS. HOOD: That's correct, your Honor.

7 MR. A. LAKIND: Okay.

8 THE WITNESS: Well, typically when you're looking at
9 breakpoints you're looking at what happens to the total fee
10 paid by a fund holder, as the size of the fund or assets under
11 management increases. And one can compute what savings arise
12 from a breakpoint by looking at what the fees would be if
13 there wasn't a breakpoint, and comparing them to what the fees
14 are with a breakpoint, and that difference is an economy
15 arising from the breakpoint.

04:57

16 BY MS. HOOD:

17 Q. And these are analyses that you performed in the past?

18 A. Yes.

19 Q. Okay. Again, we may have covered some of this through
20 your prior experience, but could you describe for the Court
21 what your experience is as it pertains to mutual fund fees?

04:57

22 A. Well, as I indicated it's something that I've done my own
23 research on, I've refereed and edited papers on those issues;
24 I've worked as a consultant to various mutual fund complexes
25 on those issues; and as I mentioned, I've been a consultant to

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1 the chief economist of the SEC on those issues.

2 Q. And with respect to the risks that investment manager
3 managers like FMG may face, what, if anything, is your
4 experience in that area?

04:58 5 A. Well, most recently looking at various entities that
6 are -- that come under the purview of the San Francisco Fed in
7 terms of analyzing their overall risk exposure on a variety of
8 dimensions, including operational risks as they pertain to
9 both their banking activities, as well as their non-banking
04:58 10 activities.

11 MS. HOOD: Your Honor, defendants at this time offer
12 Dr. James as an expert in economics, and submit that he is
13 qualified by reason of his experience and training and
14 specialized knowledge to offer opinions in this case in --
04:59 15 with respect to four main areas: Whether plaintiffs' experts
16 have demonstrated that FMG realizes any economies of scale
17 with respect to the funds at issue; secondly, the extent to
18 which any such economies of scale have been shared by FMG with
19 fund investors through breakpoints in the fund's fee
04:59 20 schedules; third, the level of the fund's fees, the fees for
21 the funds at issue and how they compare to fees charged to
22 other mutual funds in the marketplace; and finally, the risks
23 that FMG as an investment manager faces with respect to
24 servicing the funds.

04:59 25 THE COURT: All right, thank you.

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1 Any objections, Mr. Lakind?

2 MR. A. LAKIND: Yes, your Honor, might I voir dire
3 the witness?

4 THE COURT: You may voir dire the witness.

04:59 5 So, it's 3:52.

6 (VOIR DIRE ON QUALIFICATIONS BY MR. A. LAKIND:)

7 Q. Good afternoon, Mr. James.

8 A. Good afternoon.

9 MR. A. LAKIND: May I proceed, your Honor?

05:00 10 THE COURT: You may.

11 Q. Mr. James, other than in this case, you have never been
12 called upon to assess the types of risks confronted by
13 investment managers in the mutual fund industry; is that
14 correct?

05:00 15 A. No, that's not correct.

16 Q. Other than this case, have you ever been called upon as
17 an expert witness to assess whether -- strike that. You're
18 not offered in that area; I'm sorry.

05:00 19 Have you ever been retained to do any work in
20 connection with a sub-advised mutual fund?

21 A. Have I ever been retained to do any work with respect to
22 a sub-advised mutual fund?

23 Q. Yes, sir.

24 A. Yes.

05:00 25 Q. And what was that work?

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1 A. In terms of the consulting work that I did on a couple of
2 complexes looking at various fee structures as it pertains to
3 both their advisory role and the sub-advisors that they
4 retained.

05:01 5 Q. Have you had occasion to author any publications dealing
6 with sub-advised mutual funds?

7 A. No.

8 Q. Have you ever testified in a case in connection with a
9 sub-advised mutual fund?

05:01 10 A. I have not.

11 Q. Have you ever been -- strike that.

12 Have you ever been called upon to assess the
13 relationship between the fees and services provided by a fund
14 advisor in comparison to the fees and services provided by a
05:01 15 sub-advisor?

16 A. Just for point of clarification, when you say called
17 upon, do you mean as an expert witness?

18 Q. Yes, sir, as an expert witness.

05:01 19 A. Yes, I've done those in consulting activities; I haven't
20 testified in court as an expert witness on that issue.

21 Q. Have you ever been called upon to assess whether
22 economies of scale exist in connection with the management of
23 a sub-advised mutual fund?

05:02 24 A. Again, I've not testified in court on that issue; I
25 certainly examined that issue in other cases.

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1 Q. In how many occasions?

2 A. Two or three as I recall.

3 Q. And for what purpose?

4 A. It was in the context of -- when you say called upon, in
5 the context of serving as an expert witness.

6 Q. Have you ever had occasion to author any publications
7 dealing with variable annuities?

8 A. No.

9 Q. Have you ever had occasion the testify as an expert in
10 connection with variable annuities?

11 A. I'm sorry?

12 Q. Have you ever had occasion to testify as an expert in a
13 case involving variable annuities?

14 A. I don't believe so.

15 Q. Now, you have also been an expert in bankruptcy cases; is
16 that correct?

17 A. That's correct.

18 Q. And you've been an expert in real estate matters; is that
19 correct?

20 A. That's correct.

21 Q. And in consumer fraud matters?

22 A. That's correct.

23 Q. You've been an expert in product liability matters?

24 A. That's correct.

25 Q. And you've been an expert in pharmaceutical matters?

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1 A. I have.

2 Q. And you've testified as an expert in healthcare matters?

3 A. That's correct.

4 Q. And you're an employee of Cornerstone, are you not?

05:03 5 A. I'm an advisor to Cornerstone, I'm not an employee.

6 Q. In connection with your work in this case, you billed

7 about \$200,000; is that correct?

8 A. I believe at the time of my deposition it was around 200.

9 Q. And what is it today, do you know?

05:03 10 A. Maybe another hundred hours, or so.

11 Q. And your compensation from Cornerstone is about \$1.1

12 million annually?

13 A. That's correct.

14 Q. And you also have a note where Cornerstone owes you

05:03 15 somewhat over a million dollars; is that correct?

16 A. That's correct.

17 Q. And is the payment of that note contingent in any way on

18 the outcome of any expert witness work that you do?

19 A. No.

05:03 20 Q. Prior to testifying today -- I'm sorry. Roughly what

21 percentage of your professional time in the last five years

22 has been devoted to the study of issues relating to investment

23 companies?

24 A. Percentage of my professional time?

05:04 25 Q. Yes, sir.

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1 A. 10 or 15 percent.

2 Q. Last four years have you ever testified in any case
3 involving mutual fund fees?

4 A. Yes.

05:04 5 Q. And on how many occasions?

6 A. I believe on three different occasions.

7 Q. Sir, you're familiar with 15(c) material, are you not?

8 A. Yes.

05:04 9 Q. And have you reviewed all of the 15(c) material that's
10 the subject of this case?

11 A. I'm not sure what you mean by all of the 15(c) material;

12 I've reviewed 15(c) material.

13 Q. But you culled the material that you thought was relevant
14 and clearly did not review everything; is that correct?

05:04 15 A. I'd have to look at the material to tell you which of it
16 I looked at and which of it I didn't, but I don't -- I've
17 reviewed a lot of 15(c) material.

18 Q. There's some portion you did not review --

19 A. I think that's fair.

05:05 20 Q. Okay. Did you review all of the deposition transcripts
21 in this case in their entirety?

22 A. No.

23 Q. Did you read all of the Board minutes in this case in its
24 entirety?

05:05 25 A. No, I reviewed a number of deposition transcripts and a

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1 number of Board minutes, but I can't say I looked at all of
2 the depositions in their entirety or all of the Board minutes
3 in their entirety.

4 Q. Now, you do have the ability to quantify the risks which
5 a mutual fund confronts; is that correct?

6 A. I think that's true, yes.

7 Q. And have you undertaken to quantify the risks that the
8 mutual funds confront in this case?

9 A. I haven't been asked to do a quantification; I've
10 identified the nature of the risks, and believe they're
11 significant, but I haven't been asked to quantify those risks.

12 Q. Have you undertaken to quantify the risks confronted by
13 -- strike that.

14 You do have the ability as well to quantify the risks
15 confronted by an investment manager; is that correct?

16 A. Yes.

17 Q. And you have not done that in this case either; is that
18 correct?

19 A. I haven't been asked to provide a quantification.

20 Q. To your knowledge is there any peer-reviewed literature
21 that identifies the risks borne by mutual fund advisors?

22 A. Specifically with respect to mutual fund advisors,
23 nothing comes to mind. There are publications, I have one of
24 them that's widely cited, that look at business risks for
25 financial institutions generally. And those same procedures,

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1 be it for a bank or insurance company or asset management
2 firm, I think from an economic perspective are applicable to
3 across those institutions.

4 Q. Is there any peer-reviewed literature that explains how
5 the concepts that are relevant to the financial institutions
6 you spoke about are also relevant to the mutual fund industry?

7 A. Certainly what I've written on, for example, risk
8 adjusted return on capital, is -- is -- applies to mutual fund
9 management, I've applied it to mutual fund management.

10 Q. Are there any peer-reviewed studies of how to measure
11 risk in the mutual fund industry?

12 A. In terms of operational risks?

13 Q. Yes, sir.

14 A. Because certainly there are lots of risks, such as market
15 risks and investment risks that I've refereed and have
16 published articles on measurement of those types of risks.

17 With respect to specific operational risks, I think it's more
18 generic to financial institutions generally.

19 Q. Your hypothesis that mutual fund -- you have hypothesized
20 in your report that mutual fund companies confront certain
21 types of risk, operational risks and so on; is that correct?

22 A. Yes, and I provided evidence of those risks.

23 Q. Are you aware of any criteria that exists that one could
24 test that hypothesis?

25 A. Well, by looking at, for example, costs incurred for a --

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05:09 1 quite recently was in the Wall Street Journal, the problems at
 2 Third Avenue, an asset management group, in which because of
 3 investments and certain illiquid securities, the reputational
 4 consequences were I think somewhere in the order of, in terms
 5 of total outflow, three and a half billion or thereabouts. Is
 6 that my recollection? It was just this January.

 7 Q. I was asking a somewhat different question. The question
 8 I was interested in is, are you aware of any criteria that is
 9 available to test the hypothesis that mutual funds confront
05:09 10 operation risks?

 11 A. And I was prescribing how one goes about doing that,
 12 okay; by looking -- some of the risks are risks that arise
 13 infrequently. So, for example, the risks that mutual funds
 14 faced when there was a large outflow from money market funds
05:09 15 and break-the-buck issues that arose. So one looks at what
 16 the costs that were incurred by those institutions were
 17 associated with the manifestation of that risk, to give a
 18 sense of the quantification and the magnitude.

 19 Certainly, for example, in my report I talk about and
05:10 20 identify through litigation tracker, a variety of settlements
 21 in litigation related matters that mutual funds have been
 22 subject to, that informs me of the -- both not only the
 23 frequency, but the potential magnitude. Which is a real cost
 24 of doing business that needs to be considered.

05:10 25 And there are regulatory standards in the banking

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1 industry and some proposed for investment management, asset
2 management funds, to -- to address those real costs.

3 Q. Okay. Thank you, Mr. James.

4 MR. A. LAKIND: Your Honor, if I might, with regard
5 to the proffer of the witness, plaintiffs have no objection to
6 the witness' credentials on certainly economies of scale,
7 comparable fees; the description of economics in general, if
8 that's meant to go beyond those, I would hope we can get a
9 somewhat more precise explanation. If that's meant to be just
10 what was said after that, certainly we have no objection.

11 We would object to any testimony from this witness
12 on risk for two reasons. Number one, risk could be
13 quantified, and the witness has not undertaken to quantify the
14 risk. Whether or not any institution incurs risk is not
15 really -- would be appear to be a subject of expert testimony.

16 Secondly, the witness was asked if he is aware under
17 -- I didn't cite *Daubert*, but of any criteria that might be
18 used to testify -- excuse me; to test whether a risk exists,
19 and it doesn't appear that there is any such criteria. So,
20 specifically we would object to any testimony about risk from
21 this witness.

22 THE COURT: Risk, okay.

23 Ms. Hood, do you wish to be heard?

24 MS. HOOD: Yes, please, your Honor. My
25 understanding from Mr. Lakind is that the only -- the only

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05:12 1 topic of the four topics I went through earlier that
 2 plaintiffs have an objection to is Dr. James' testimony or
 3 contemplated testimony on risk faced by investment managers.
 4 And the basis that Mr. Lakind just gave -- one of the two
05:12 5 bases for why Dr. James should not be qualified in that area
 6 is because it's possible to quantify risk, but Dr. James
 7 hasn't done that here.

 8 Dr. James concedes as he just testified he wasn't
 9 asked to quantify it here. He looked exclusively at the
05:13 10 nature of the risks that an investment manager like FMG faces.
 11 And so the fact that he hasn't taken an analysis that -- has
 12 not taken that analysis one step further to quantify the risks
 13 has nothing to do with his qualifications to offer an opinion
 14 on the nature of the risks that FMG faces.

05:13 15 THE COURT: Does that answer your objection, Mr.
 16 Lakind?

 17 MR. A. LAKIND: It does not, your Honor. Because
 18 the second part of the objection dealt with is there criteria
 19 available to ascertain whether or not mutual funds sustain
05:13 20 risk, and I believe that is one of the *Daubert* factors.

 21 THE COURT: Okay.

 22 MS. HOOD: May I be heard, your Honor, on that
 23 second argument?

 24 THE COURT: You may.

05:13 25 MS. HOOD: So, Mr. Lakind asked Dr. James twice

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05:14 1 about the standards and whether there are any standards that
2 could be applied to analyze the risks in this context, and he
3 gave an explanation that there are standards out there,
4 standards that he would uses as an economist. And so again
5 this isn't a basis for disqualifying Dr. James with respect to
6 this issue.

05:14 7 THE COURT: All right. So my view of it is that
8 I've listened to Dr. James' credentials. He's a professor at
9 two universities, University of Michigan and -- I'm sorry; the
05:14 10 Universities of Cambridge and Florida; he's also taught at
11 other colleges, like Michigan State and University of
12 Michigan; he's been a consultant for some type of settlement
13 between the Janus Fund that he oversaw, and he reviewed
14 different issues concerning what the Securities and Exchange
05:14 15 Commission may see as a legitimate basis for allocation of
16 settlement proceeds, as opposed to what Janus may think.

05:15 17 He's also been selected to work with the chief of
18 economics I believe of the Securities and Exchange Commission;
19 he worked on the pricing of mutual funds; he worked on
05:15 20 economies of scale as a consultant to certain mutual funds;
21 he's also indicated some information with regard to how you go
22 about in analyzing economies of scale; and then there was some
23 discussion with regard to risks.

05:15 24 But, at any rate, my view is in looking at the Rule
25 703: A witness who is qualified as an expert by knowledge,

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1 skill, experience, training or education may testify in the
2 form of opinion or otherwise, if, the expert's scientific,
3 technical or specialized knowledge will help the trier of
4 fact; Mr. James has met that factor.

05:16 5 The testimony is based on sufficient facts or data;
6 it appears to me that Mr. James has a substantial amount of
7 facts and data from all his years of being on these editorial
8 boards of economic magazines and journals; he's also been with
9 the SEC -- I shouldn't say been with; but has been retained by
05:16 10 them on mutual fund matters. He's also been with the Federal
11 Reserve in San Francisco, and he seems to have reviewed such
12 matters there. So, based on that, there seems to be
13 sufficient facts.

14 I also think that based on what I've heard, the
05:16 15 testimony will be the product of reliable principles and
16 methods; which he has indicated that most of his research has
17 been about how go about testing for this or how you analyze
18 that. So, I'm certain he will present those reliable
19 principles.

05:17 20 And lastly, the issue comes down to risk. And it
21 seems to me with the risk and the nature of those risks as
22 opposed to the quantity of those risks, would be something he
23 would have learned from his prior expertise, so I'll allow
24 that.

05:17 25 And then lastly, although we didn't really go over

05:18 1 it too much, the expert must reliably apply the principles and
2 methods to the facts of the case, which I'm certain is going
3 to be -- or hopefully will be his testimony today. So, based
4 on those four factors, I'll allow the testimony, and Mr. James
5 is qualified to be an expert.

6 MS. HOOD: Thank you, your Honor. And before I
7 proceed, I just note that it looks as if we're about 10
8 minutes passed 4:00 right now, and I'm happy to continue if
9 that's your preference.

05:18 10 THE COURT: That's a good point; why don't we break
11 for the day, and we'll restart tomorrow at 10:30.

12 So, let me just go over the time for today. So, Ms.
13 Hood, you had your voir dire from 3:22 the 3:52, so you had a
14 half hour. And Mr. Lakind, you went from 3:52 to 4:05, which
05:18 15 is 13 minutes. I think we're gearing for an and a half hour
16 per witness; isn't that right, Mr. --

17 MR. MURPHY: Something like that. There may be a
18 little fluidity there, but I think if we keep it as 50/50
19 we're still on target to finish Thursday afternoon.

05:19 20 THE COURT: All right, thank you.

21 So, you may step down, Mr. James, we'll see you in
22 the morning.

23 THE COURT: Have a good evening.

24 (Counsel say thank you.)

05:19 25 (Proceedings concluded for the day.)

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